# Credit Union Development in Ukraine: Options and Strategies for USAID/Kiev

*Final Report*

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John H. Magill
Colleen E. Green

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DAI
7250 Woodmont Avenue, Suite 200, Bethesda, Maryland 20814

# PREFACE

The U.S. Government, through the U.S. Agency for International Development (USAID/Kiev), has supported the promotion and strengthening of credit unions in Ukraine since 1993—first with a small grant to the World Council of Credit Unions of $300,000 to promote credit unions and train credit union organizers, and later with a grant of $1.0 million in 1995 for technical assistance, training, and other support to the fledgling movement. Services provided under the second grant ended in September 1999. USAID/Kiev is interested in providing further support to credit union development in the country. Experiences with the previous two grants, however, suggest that a major change in focus and direction is required to have a significant impact on the viability and success of the credit unions system in Ukraine.

USAID/Kiev contracted Development Alternatives, Inc. (DAI) through Task Order OUT-PCE-I-808-99-00009-00 to conduct an assessment of experiences to date, examine the current status and problems of the credit union system, and provide information to USAID/Kiev that would assist in the formulation of an effective program to further credit union development in the country. A team consisting of John H. Magill and Colleen E. Green spent approximately one month in Kiev reviewing project documentation and interviewing representatives from USAID/Kiev, other donor agencies and projects, the Ukrainian National Association of Savings and Credit Unions, and select local credit unions. A list of persons contacted is contained in Appendix A. This report summarizes the findings of that assessment and is submitted in fulfillment of Task Order OUT-PCE-I-808-99-00009-00.

The team wishes to thank the staff of USAID/Kiev, the staff and elected officials of the Ukrainian National Association of Credit Unions, staffs and elected officials of the credit unions that were visited, officials of donor agencies, and consultants from other projects working with credit unions for their cooperation and assistance during the course of the assessment. The conclusions and recommendations presented in the report, however, are those of the consultants and should not be considered to represent the positions or opinions of any of these organizations.

# ACRONYMS

Currency Equivalents:
1 U.S. Dollar = 5.4 Ukrainian Hryvna (UAH)

| | |
|---|---|
| CCA | Canadian Co-operative Association |
| CIDA | Canadian International Development Agency |
| CU | Credit union |
| CUTC | Credit Union Training Center |
| EBRD | European Bank for Reconstruction and Development |
| ENI | Europe and the Newly Independent States |
| GDP | Gross domestic product |
| IAS | International accounting standards |
| IBRD | International Bank for Reconstruction and Development (World Bank) |
| IFC | International Finance Corporation |
| IMF | International Monetary Fund |
| IOM | International Organization for Migration |
| IPC | International Projekt Consult |
| KfW | Kreditanstalt für Wiederaufbau |
| MSME | Micro, small, and medium-sized enterprises |
| NBU | National Bank of Ukraine |
| NewBizNet | Development of Support Networks to Assist New Small and Medium-Scale Business |
| NGO | Nongovernmental organization |
| PEARLS | WOCCU's Financial Monitoring System (Protection, Effective Financial Structure, Asset Quality, Rates of Return and Costs, Liquidity, and Signs of Growth) |
| PVO | Private voluntary organization |
| RFA | Request for Assistance |
| SME | Small and medium-sized enterprise |
| TACIS | Technical Assistance to the Commonwealth of Independent States |
| TOT | Training of trainers |
| UAFDF | Ukraine Agriculture Finance Development Foundation |
| UAH | Ukrainian hryvna (local currency) |
| UNASCU | Ukrainian National Association of Savings and Credit Unions |
| UMREP | Ukraine Market Reform Education Project |
| UNDP | United Nations Development Programme |
| USAID | U.S. Agency for International Development |
| WB | World Bank (see IBRD) |
| WOCCU | World Council of Credit Unions |

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# EXECUTIVE SUMMARY

The U.S. Government, through the U.S. Agency for International Development (USAID/Kiev), has supported the promotion and strengthening of credit unions in Ukraine since 1993—first with a small grant to the World Council of Credit Unions (WOCCU) of $300,000 to promote credit unions and train credit union organizers, and later with a grant of $1.0 million in 1995 for technical assistance, training and other support to the fledgling movement. Services provided under the second grant ended in September 1999. USAID/Kiev is interested in providing further support to credit union development in the country. The purpose of this assignment was to assess credit union development in the Ukraine, examine the current status and problems of the credit union system, and provide information to USAID/Kiev that would assist in the formulation of an effective program to support further credit union development in the country.

## FINDINGS AND CONCLUSIONS

The modern credit union movement in Ukraine is young. All credit unions currently operating in the country were formed after the collapse of the Soviet Union, and most are less than four years old.

Credit unions operate under a presidential decree entitled the "Temporary Statement on Credit Unions in Ukraine" from September 1993, which contains a number of serious legal weaknesses that make it inadequate for regulating and supervising the credit union movement. These weaknesses include:

- A weakly defined organizational structure, which designates them as not-for-profit entities but does not define their tax status;
- An absent regulatory and supervisory structure;
- A weakly defined operational structure that empowers them to operate under the law but does not specify their powers (e.g., ability to loan and borrow from other credit unions); their services (e.g. definition of savings versus shares); or their internal legal structure (e.g, differentiate them from investment clubs or pyramid schemes); and
- A lack of minimum requirements regarding start-up capital, ownership, and operating standards.

More than 400 "credit unions" have registered with the National Bank of Ukraine (NBU) under this decree since 1992.

Because the credit union movement is young, both the "affiliated" movement[1] itself and the individual credit unions that comprise it are small. At the time of the 2000 annual general meeting of the Ukrainian National Association of Savings and Credit Unions (UNASCU), 95 of the country's 400 or so registered credit unions were affiliated with the national association. More than half of these credit unions have assets of less than UAH 65,000 (US$12,000).[2]

In spite of the fact that the credit union movement in Ukraine is young, small, and poorly regulated, growth has been impressive during the past eight years. The 95 credit unions affiliated with UNASCU have approximately 60,000 members and total assets of approximately UAH 10.6 million (US$1.96 million). This represents substantial growth from the 52 credit unions with 17,750 members, UAH 2.2 million (US$1.2 million) in assets, and UAH 1.9 million (US$1.0 million) in loans outstanding that existed at year-end 1996.[3] This growth in assets and loans is especially impressive because it is based almost entirely on member savings and deposits—donor contributions to capitalization and portfolio have been very small.

Credit unions have demonstrated that they have found a viable niche in the financial market place. They play an important role in mobilizing savings and meeting personal loans requirements of a sector of the population that lacks access to financial services and that can make effective use of access to those services. Most important, credit unions have the potential for making a major impact on the financial well-being of a sizeable sector of the country's population, and particularly on the lives of women.

The credit union movement, however, faces a number of problems and constraints. It is small, undercapitalized, and lacks the structure and facilities to perform the tasks expected of it. Leaders and credit union staffs are new to credit unions and to provision of financial services, and they lack the skills necessary to operate credit unions as modern financial institutions.

On the legal side, credit unions ultimately require adequate legislation and regulation. Credit unions operate under a presidential decree that, while affording the legal right to organize and operate, does not adequately protect credit union identify, interests, and operations. Organizations such as investment funds and pyramid schemes have organized under the name of "credit unions." The decree does not provide adequate standards for capitalization or for safety and soundness. It also does not provide an unambiguous tax-exempt status for credit unions. And, it does not provide for regulation and supervision. Although credit unions can operate successfully in the short run with self-regulation, in the long run a more permanent legal framework needs to be enacted.

These problems, while real, are amenable to improvement through external support. In particular, external support can help impart a modern "vision" to credit union leaders and staffs. It can help

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[1]The "affiliated" credit union movement consists of those credit unions that belong to and pay dues to the national credit union association.
[2]An exchange rate of 5.4 hryvna = 1 U.S. dollar is used throughout this report.
[3]World Council of Credit Unions, "Mid-Term Evaluation," April 1998, Annex 3.

credit unions improve their internal operations so that they can better serve the needs of their members. It can help plan and develop the types of services that a national association needs to offer so that it can capture the allegiance and support of its members. It can help research and plan new services and facilities. And it can help capitalize the credit union movement.

Success in developing a viable credit union movement will be a major benefit to Ukraine. It is not unreasonable to predict a credit union movement of 300 credit unions, 500,000 members, and assets in excess of US$50.0 million within five years, with proper assistance.

## RECOMMENDATIONS

USAID/Kiev should strongly consider future support to developing the credit union movement and system in the Ukraine. Proper support can greatly accelerate growth, solidify the foundation of the credit union system, and create the structures and systems that will be necessary for future expansion and soundness.

Given the current status and the major problems facing the credit union movement in Ukraine, future assistance provided by USAID/Kiev should focus on four major areas:

- Accelerating the growth of base-level credit unions, both in terms of the number of credit unions and the size and performance of existing credit unions;
- Improving the performance and sustainability of the national association, UNASCU, so that it offers a range of services and performs activities that are valuable to its membership and that strengthen its role as a democratic structure;
- Developing an adequate legal and regulatory environment for the growth of strong credit unions in the country; and
- Developing an effective structure and appropriate technologies for the functioning of a modern credit union system in Ukraine.

This assistance should be planned over a four-year period, with the first two years concentrating on building sustainable growth, strengthening UNASCU, developing the legal and regulatory framework for credit unions and, if possible, resolving the data processing problems facing credit unions. The final two years would work on sustaining momentum in sustainable growth and on supporting the implementation of two key pieces of the credit union structure—a central liquidity facility and a stabilization fund—if feasibility studies confirm the viability of these funds.

# BACKGROUND

Although nine years have passed since the break-up of the Soviet Union, Ukrainians are still plagued by the collapse of the monetary system that ensued. The loss of monetary control by the state undermined the ruble as a medium of exchange. Barter transactions increased and enterprises resorted to keeping foreign exchange earnings outside the country. This capital flight aggravated the plight of the ruble. At the same time, Ukraine introduced coupons, and later the hryvna, as a substitute currency.

Hyperinflation in the early 1990s led to major increases in the amount of money printed, which was primarily absorbed through credits to government and state-owned enterprises. Credit control was effectively nonexistent. Money presses financed the large budget deficits that resulted from the revenue losses due to a decline in economic output. In 1991, government spending increased to 48 percent of gross domestic product (GDP), while government revenue remained at 34 percent of GDP. In 1992, government spending amounted to 70 percent of GDP. In 1993, the government decided that deficit reduction did not matter and spent nearly 90 percent of its GDP, resulting in heavy credits issued by the National Bank of Ukraine (NBU) to the government.

Roughly 60 percent of the population had to grow their own food, and many people had two or more jobs. It was estimated that about 60 percent of private business transactions fell outside of the official tax rolls, largely due to high taxation on business profits.

Ukraine replaced its mono-bank system with a two-tier banking system: the Central Bank no longer made commercial loans, and commercial and quasi-commercial banks took over financial intermediation. Most of the commercial banks remained under state ownership, however, and inherited the deposits and loans of the mono-bank system. The Ukrainian banking system is still small and weak by Western standards, consisting of approximately 160 banks and about UAH 25 billion (about US$5 billion) in total assets.[4]

Because banks inherit many loans made to insolvent companies, a large proportion of bank loans were non-performing. Poor quality loan portfolios were not readily revealed, and enforcement of financial discipline was inefficient. Continued channeling of credit into insolvent companies made credit scarce to profitable enterprises and nonexistent to individual consumers. Ineffective payments systems, extensive delays in clearing transactions, and lack of effective competition forced businesses and households to hold large amounts of cash for transaction purposes.

Household financial needs were largely ignored under the Soviet system. Some individuals and households maintained limited savings in the Oschadny (state savings bank) system, but most people converted their meager savings from local currency to U.S. dollars and other hard currencies, preferring to keep it hidden at home and in other undisclosed locations. The bulk of consumer transactions took place in cash, bypassing the weak banking system.

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[4]Based on information from the Draft Final Report entitled “Background for Financial Markets Development in Ukraine” and presented to USAID by Financial Markets International, Inc. January 2000.

Before 1992, there were no officially registered credit unions in Ukraine, although two forms of informal credit systems existed during the Soviet era. One of these, called a *chornaya kassa* ("black kassa"), was a Soviet version of a rotating savings and credit association. These "black kassas" were formed voluntarily, usually by a group of people working in the same division at an industrial enterprise. Group members pooled a certain portion of their monthly salaries, and each member had the opportunity to use the total pooled funds for whatever purpose desired during his or her turn. The borrower only needed to repay it at the end of the given period. Generally, loan amounts were small, and group members used them to buy consumer goods or pay for vacations. Loan terms generally ranged from one to three months, although loans for up to six months were given on extraordinary occasions. The second form were mutual aid funds (*kassa vsaemopomishi*), which were similar to the "black kassas," although more formal. These funds were generally administered and monitored by an official at a large enterprise for other employees at the enterprise. "Black kassas" and mutual aid funds generally worked well because they were small and based on relationships of trust.

By 1992, with the help of U.S. and Canadian organizations, the credit cooperative movement was born and the first wave of modern credit unions began to appear.

The U.S. Government, through the U.S. Agency for International Development (USAID/Kiev), first began to support the promotion and strengthening of credit unions in Ukraine in 1993 with a small grant to the World Council of Credit Unions (WOCCU) of $300,000 to support the initial promotion of credit unions and to provide training to organizers of new credit unions. At that time, the average Ukrainian citizen had little or no access to personal financial services. Increased competition was urgently needed to boost financial market efficiency not only by expanding the availability of savings instruments to the mass market but also by increasing the supply of loanable funds to the average citizen for both productive and consumer purposes. USAID/Kiev and WOCCU determined that improvements could best be achieved by establishing a credit union system.

In September 1995, USAID/Kiev awarded a three-year grant[5] in the amount of $1.0 million to WOCCU to provide three years of technical assistance, training, and other support to the fledgling movement. The broadly stated objective of the grant was to improve the availability of financial services to individuals and communities in Ukraine that did not have access to these services by forming at least 10 safe and sound credit unions capable of delivering efficient and high quality savings and credit services to their members. Program objectives included introducing project credit unions to strategic and business planning, financial management systems and policies, marketing and promotion, risk management, savings administration, credit administration, delinquency control and collection systems, automated accounting and reporting systems, payment of real returns on savings and charging of market rates on loans, and application of safe and sound business practices and prudential standards. It was expected that 20,000 members would be using the services of project credit unions by the end of the project. In addition, 875 members were to receive training in member responsibilities, democratic control, and basic savings principles and practices. Legislation, prudential supervision, and rules and

[5]Later this was extended to four years.

regulations were to be strengthened to enable credit unions to grow while protecting members' savings and ensuring accountability and safety

In pursuit of this objective, WOCCU initially concentrated on establishment of new credit unions, implementation of credit union internship and U.S. volunteer programs, computerization of management and accounting systems, financial intermediation, and legislative policy dialogue. Following a mid-term evaluation in February 1998, WOCCU's activities were refocused on improving the financial performance of 11 individual model credit unions, selected in consultation with the Ukrainian National Association of Savings and Credit Unions (UNASCU), as the most critical condition for rapid financial and organizational growth.[6] In addition, WOCCU was instrumental in providing institution-building support to UNASCU. Specifically, WOCCU:

- Focused on improving internal capabilities of the model credit unions in the areas of strategic and business planning, financial management systems and policies, marketing and promotion, risk management, savings administration, credit administration, delinquency control, and collection systems; and
- Provided UNASCU with resources, training, and systems needed to represent the interests of credit unions, improve credit union legislation and regulations, and create a united credit union system.

The WOCCU activity achieved the following during the four-year period: (1) installation of the PEARLS[7] monitoring system; (2) introduction of minimum prudential standards of excellence; (3) establishment of a database of financial information on project credit unions; (4) approval of tax exempt status for credit unions for purposes of passive income tax; (5) installation of a delinquency measurement tool in half of the model credit unions; and (6) provision of financial support to UNASCU.

[6]WOCCU, *Final Project Report*, January 11, 2000, p. 1.

[7] A management information system encompassing the following areas: **P**rotection, **E**ffective Financial Structure, **A**sset Quality, **R**ate of Return and Costs, **L**iquidity, **S**igns of Growth

# METHODOLOGY

The purpose of the assessment completed by the Development Alternatives, Inc. (DAI) team was to assist USAID/Kiev in understanding the current and overall environment for growth and sustainability of credit unions in Ukraine and to provide recommendations for a Request for Assistance (RFA). As specified in the Scope of Work, the team was asked to answer questions on:

- Credit union operations and environment;
- Sustainability of credit unions and the credit union movement;
- Credit union management, standards, and supervision;
- Marketing and public awareness;
- Services available to credit unions;
- Donor assistance and what has and has not been done to date;
- Gender issues; and
- Quantitative data.

The team spent approximately four weeks in Ukraine. During this time, the team reviewed secondary information—including project reports and evaluations, memoranda, and public relations materials—provided by the Mission, UNASCU, WOCCU, and others. This background material provided the framework for a series of extensive interviews with the following persons and groups:

- USAID/Kiev staff;
- Staff and board members of UNASCU;
- The former WOCCU project manager;
- Project managers from various bilateral, multilateral, and private donor institutions, including the World Bank, U.N. Development Programme (UNDP), Canadian Co-operative Association (CCA), Canadian Embassy, and International Foundation for Social Adaptation (Soros Fund);
- Leadership from Ukrainian-American credit unions in the United States;
- Staff from other USAID projects involved with credit unions; and
- Staff and management from 16 credit unions in Kiev, the Western region, and selected cities in the Eastern region.

A full list of interviewees and their contact information is presented in Appendix A. A matrix of credit union statistics and responses to questions posed by the assessment team is provided in Appendix D.

Findings, conclusions, and recommendations were discussed with UNASCU leadership, representatives of the Ukrainian-American credit union movement, and USAID/Kiev staff. A draft report consolidating the materials gathered and comments of the various organizations was prepared and submitted to USAID/Kiev on June 8, 2000. Comments on the draft report were received from USAID/Kiev on July 14. The revised final report incorporates these comments.

# CURRENT SITUATION OF THE UKRAINIAN CREDIT UNION MOVEMENT

Since the "rebirth" of credit unions in Ukraine and the 1993 presidential decree legalizing credit unions, some 400 "credit unions" have registered with the NBU. Currently, 95 of these credit unions are affiliated with the UNASCU. Little or no data are readily available on the non-affiliated credit unions; UNASCU estimates that about half of the remaining "credit unions" have ceased to operate, and many of the others are not really operating as credit unions. There is considerable fear in the movement that many of the non-affiliated credit unions are actually pyramid schemes or investment companies operating under the guise of a credit union. Terms used in this report that refer to "credit union system" or "credit union movement" or "credit unions in Ukraine" refer only to the 95 credit unions affiliated with UNASCU.[8]

## CREDIT UNIONS

The affiliated credit union movement in Ukraine is small but growing.[9] As of UNASCU's annual meeting in May 2000, the 95 credit unions affiliated with UNASCU had nearly 60,000 members, approximately UAH 10.6 million (US$1.96 million) in assets, and UAH 9.7 million (US$1.8 million) in loans outstanding. This represents substantial growth from the 52 credit unions with 17,750 members, UAH 2.2 million (US$1.2 million) in assets, and UAH 1.9 million (US$1.0 million) in loans outstanding that existed at year-end 1996.[10] It must be remembered that during this period the country suffered a major financial and economic crisis, and the hryvna depreciated 65 percent in value against the dollar.[11]

### SIZE OF CREDIT UNIONS

The 80 credit unions that reported data to UNASCU at the end of 1999 had an average of 668 members, ranging from the smallest credit union with 55 members to one exceptionally large credit union with 15,386 reported members. Excluding this one credit union, the average was 477

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[8]Because the assessment team visited only one unaffiliated credit union, it would be presumptuous to speculate on the others based on the one.

[9]Statistical data in this section are drawn from a three different sources—UNASCU's 2000 annual meeting membership list of 95 active credit unions, UNASCU's monitoring statistics for 79 credit unions reporting on March 31, 2000, and a summary table of year-end statistics for 1997 through 1999 compiled by UNASCU in which year-end 1999 data are available for 80 credit unions. However, not all credit unions reported all data for any of the years, the reporting periods differ for the various sources, and the number of credit unions for which data are available differ from year to year and from data item to data item. Apparent inconsistencies in the reported numbers are due to these differences.

[10]World Council of Credit Unions, "Mid-Term Evaluation," April 1998, Annex 3.

[11]Since Ukrainian credit unions work in the local economy, a comparison of values in dollar terms may not appear relevant. In this case, the dollar comparison is used as a proxy for an inflation adjustment as CPI data for the period are not available from the IMF publication *International Financial Statistics*.

members per credit union, with a median of 285 members. Only three credit unions reported less than 100 members. Since 50 is generally considered to be a minimum number of members for a viable credit union, the credit unions in Ukraine have sufficient members to become viable.

Although Ukrainian credit unions are fairly large in terms of number of members, they are small in terms of assets and assets per member. The 80 credit unions had an average of UAH 131,989 (US$24,442) in assets, ranging from a low of UAH 3,461 (US$641) to UAH 732,034 (US$135,562). Median assets (UAH 63,537 or US$11,766) were only about half of mean assets, which means that most credit unions are very small. In fact, 36 of the reporting credit unions had assets of less than UAH 50,000 (US$9,091), 14 had assets between UAH 50,000 and UAH 100,000 (US$18,182), 16 had assets between UAH 100,000 and 250,000 (US$45,455), 9 had assets between UAH 250,000 and 500,000 (US$90,909), and 5 had assets over UAH 500,000 (US$136,364). As can be seen in the distribution of credit unions by asset size in Table 1, 14 credit unions accounted for nearly 60 percent of the total affiliated assets.

The relatively small size of the credit unions can be seen more clearly in statistics for assets per member, which ranged from UAH 8 (US$1.48) per member to UAH 2,060 (US$381) per member. Forty-eight credit unions (61 percent of those reporting) had less than UAH 250 (US$46.30) in assets per member.

While there is no minimum asset size below which a credit union cannot become self-sufficient or viable, it is clear that small credit unions have difficulty in serving member needs and maintaining member loyalty. Small asset size means that earnings are limited, reducing the ability to pay staff, meet member demand for loans, and grow. Growth of the existing credit unions must, therefore, be a major priority of any future assistance to the credit union movement in Ukraine.

**Table 1**
**Distribution of Credit Unions by Asset Size**

| Asset Range | Number (and Percent) of Credit Unions | Percent of Total Affiliated Assets |
|---|---:|---:|
| UAH 0 – 25,000<br>(US$0 – 4,630) | 19 (24.1) | 2.4 |
| UAH 25,001 – 50,000<br>(US$4,630 – 9,260) | 17 (21.5) | 5.9 |
| UAH 50,001 – 100,000<br>(US$9,260 – 18,520) | 14 (17.7) | 9.8 |
| UAH 100,001 – 250,000<br>(US$18,520 – 46,296) | 15 (19.0) | 22.4 |
| Over UAH 250,000<br>(over US$46,296) | 14 (17.7) | 59.5 |
| Total | 79 (100.0) | 100.0 |

## REGIONAL DISTRIBUTION OF CREDIT UNIONS

UNASCU divides Ukraine's 26 oblasts[12] into four regions—Western, Southern, Eastern, and Central. UNASCU-affiliated credit unions currently are located in 22 of the 26 oblasts as follows:

Western Region — Ivano Frankivsk, Khmelnytska, Lviv, Ternopil, Vinnytsya, Volyn, Zakarpattia

Southern Region — Crimea, Kherson, Kirovohrad, Mykolaiv, Odesa

Eastern Region — Dnipropetrovsk, Donetsk, Kharkiv, Luhansk, Zaporizhia

Central Region — Cherkasy, Chernihiv, Kyiv, Poltava, Sumy

The greatest number and percentage of affiliated credit unions are found in the Western region, as can be seen in Table 2.

**Table 2**
**Distribution of Affiliated Credit Unions, by Region**[13]

| Region | Number | Percent |
|---|---|---|
| Western | 44 | 46.3 |
| Southern | 15 | 15.8 |
| Eastern | 17 | 17.9 |
| Central | 19 | 20.0 |
| Total | 95 | 100.0 |

There are at least two reasons for the heavy concentration of credit unions in the Western region. Credit unions existed in this region until 1939, which meant that many in the population already had experience with this form of cooperative. Also, substantial Canadian-Ukrainian assistance, supported by the Canadian International Development Agency (CIDA), has been concentrated on developing credit unions in the Western region.

There are substantial regional differences among the credit unions. Credit unions in the Western region tend to be smaller in terms of assets and assets per member than credit unions in the rest of the county (see Table 3). Credit unions in the Southern region tend to be larger than credit unions elsewhere. Statistics for the Eastern region are distorted by the presence of one very large (in terms of membership) credit union.

**Table 3**

[12]Including the Kiev administrative district and Crimea.
[13]Data provided by UNASCU from 2000 annual meeting statistics.

**Averages per Credit Union, 12/31/99**

| Region | Members | Assets | Assets/Member |
|---|---|---|---|
| Western | 481 | 95,715 | 208 |
| Southern | 538 | 252,683 | 413 |
| Eastern | 1,648 | 179,784 | 309 |
| Central | 265 | 112,664 | 427 |
| Nation-wide | 668 | 131,989 | 296 |

## URBAN-RURAL DISTRIBUTION

Credit unions in the Ukraine are primarily an urban institution, as 60 of the 95 credit unions affiliated with UNASCU are located in urban areas. Only 26 of the 60 urban credit unions are located in the five largest cities in Ukraine, however, which shows good distribution of credit unions between large and small cities. Western Ukraine has the highest number of rural-based credit unions, with 59 percent of the credit unions in that region classified as rural. In contrast, only six credit unions in the other regions were classified as rural.

The greater concentration of rural credit unions in the Western region may be due to the promotion practices of the Canadian program, which encouraged model credit unions to assist in the creation of additional credit unions in nearby towns. These new credit unions tended to be in areas designated as "rural."

Data from year-end 1999 show that rural credit unions are significantly smaller than urban credit unions. Rural credit unions had an average of 476 members per credit union compared to an average of 768 members for urban credit unions. Of greater significance was the difference in asset size and assets per member. Rural credit unions had an average of UAH 93,201 (US$17,260) in assets and an average of UAH 202 (US$37.41) in assets per member, compared to an average of UAH 150,665 (US$27,900) in assets and UAH 342 (US$63.33) in assets per member for urban credit unions. These differences in size may be because rural credit unions are relatively younger than urban ones, or it may because of lower incomes in rural areas. Because rural credit unions are small, they are not good candidates for managing high-risk rural production credit loans for donor programs.

## GROWTH

The Ukrainian credit union movement is small but growing. According to statistics provided by UNASCU, membership in affiliated credit unions grew from 27,100 to 52,100 between year-end 1997 and year-end 1999, and to approximately 60,000 by the date of the annual general meeting on May 27, 2000. During the same period, total assets increased from UAH 4.4 million to UAH

10.6 million, loans increased from UAH 3.4 million to UAH 9.7 million, and deposits (not including share deposits) increased from UAH 3.6 million to UAH 6.5 million.[14]

Credit union growth potential is largely determined by the defined “field of membership” of each credit union. Credit unions accept members from a well-defined field of membership, called a “common bond,” based on the community in which members live, employment by a specific firm or industry, or membership in a common group. Credit union growth potential is initially determined by the size of this common bond. Penetration rates, defined as the number of members divided by the total eligible population of the field of membership, are still very limited in most credit unions, leaving substantial opportunities for short- and long-term growth.

Because of the high rate of inflation and the financial crisis of 1998, however, real growth in financial indicators has actually been negative during 1997 to 1999. In dollar terms, assets decreased from US$2.3 to US$1.96 million, deposits fell from US$1.9 to US$1.2 million, and loans remained almost constant during that period.[15] During 1999, the year following the financial crisis, real growth in assets, savings, and loans was positive and substantial.

## SELF-SUFFICIENCY

The individual credit unions are financially weak, although most are covering expenses with income. Of the 79 credit unions reporting data regularly to UNASCU, 58 were completely covering expenses from earned income, while 21 were not.[16] Twenty-one credit unions (not the same 21 as reporting losses) had net loss carry-forwards—some from having purchased equipment in advance of having income, and others because of delinquency problems.

Self-sufficiency should be relatively easy to achieve, even at relatively low asset levels because of the very high interest rates charged on loans and the large spreads between deposit and loan rates. Interest rate spreads at the credit unions visited by the assessment team ranged from as low as 0.3 percent per month to as much as 3.0 percent per month, with an average interest rate spread of 2.46 percent per month (approximately 30 percent on an annual basis). Pricing of services—deposit as well as loan—is an area in which credit union boards, managers, and staffs need further assistance and training.

## DELINQUENCY

Delinquency statistics are somewhat suspect because of a lack of standard definitions and the team’s inability to verify the data. Of the 79 credit unions reporting information for March 31, 2000, 27 reported no delinquency at all, 14 reported delinquency rates of less than 5 percent, 8 reported delinquency rates of between 5 and 10 percent, and another 10 reported delinquency rates of between 10 and 20 percent. If these figures are accurate, 52 percent of the credit unions

[14]UNASCU statistics on credit union members, assets, loans and deposits.
[15]Expressing values in dollars provides an approximation of the effect of inflation in the absence of reliable CPI data.
[16]Quarterly statistic reported by credit unions to UNASCU, March 31, 2000.

had delinquency rates of less than 5 percent, and 62 percent had delinquency rates of less than 10 percent.

At the same time, however, nine credit unions reported delinquency rates of greater than 40 percent, and one even had a delinquency rate in excess of 99 percent.

Because of the importance of delinquency management and control to the viability and sustainability of a credit union, more attention needs to be paid to standardizing these data, improving delinquency management skills among credit union managers, and providing prompt and effective follow-up to credit unions that are having problems managing delinquency.

## WOMEN IN CREDIT UNIONS

Because of their often close links to the community, credit unions tend to have a high participation of women both in their management and organization and their membership. Women often make up the majority of credit union employees and management, and they play lead roles on boards of directors, supervisory boards, and credit committees. Of the 16 credit unions visited by the team, 54 percent of the total membership of the 16 credit unions were women, 56 percent of the executive directors were women, and a majority of board members were women. According to UNASCU statistics, approximately 55 percent of the members of affiliated credit unions are women.

Credit unions do not engage in gender analysis. Credit unions also do not currently disaggregate gender information, except as required by the international donor programs with which they are affiliated. A number of credit unions, however, are focused on addressing women's business issues, as their membership is made up of women's organizations. Overall, the assessment team felt that inclusion of women in the credit union movement was strong, with women participating at all levels of the credit unions and their management.

## STRENGTHS AND WEAKNESSES OF THE CREDIT UNIONS

The major strength of the credit unions in Ukraine is that the growth of a core group of financial institutions that are functioning as true credit unions has reached a stage of development that appears to be sustainable. Regardless of whether or not future assistance is provided to support credit unions in the country, the current movement has reached a stage where it will continue to grow on its own. This is accompanied by a cadre of dedicated and highly motivated staffs and leaders who appear committed to furthering the development of credit unions and the credit union system.

At the same time, however, credit unions are still very young in Ukraine. In spite of impressive growth and development, there are still very few "real" credit unions, and they serve only a small fraction of the population. Credit unions are small—the largest credit union affiliated to UNASCU has only UAH 732,000 (US$136,000) in total assets. Penetration, even into defined fields of membership, is still limited. The main problems facing credit unions in Ukraine stem from their youth and small size.

Perhaps the major factor constraining the growth of credit unions is the timid approach to growth on the part of many, if not most, boards and staff, and the lack of vision among credit union leaders as to the growth potential of their credit unions. Few of the individuals interviewed had a clear concept of the role their credit union should play in either the local community or the financial lives of their members. No leader interviewed had the vision of the credit union as growing to become a full-service personal financial institution. Few were aware of penetration rates[17] or expressed a desire to increase penetration of their primary fields of membership to significant levels. Many were afraid to stimulate growth because they were not convinced they would be able to handle the increases in funds. Others were reluctant to open membership to a broader field of membership.[18] This absence of a vision of the credit union as an innovative and aggressive financial institution serving a broader range of personal financial needs is largely due to the lack of direct exposure of the leaders to successful credit union systems and models: those who have traveled and had the opportunity to witness firsthand the operation of credit unions elsewhere are more aware of the possibilities than those who have not.

This lack of vision and commitment to growth is also partly the result of limited experience in credit union management and underdeveloped leadership skills. General skills in financial management and management of a credit union as a financial institutions are weak. In particular, delinquency management and control are still problems in many credit unions. The assessment team also noted numerous instances of credit union actions that place the assets of the credit unions at risk—financing book publications, cross-subsidization of services using credit union earnings to finance social projects, and others. Credit union leaders have been in their roles for a limited amount of time and have been exposed to limited training and preparation. Continual training and upgrading of management skills are needed to develop confidence in managing and operating credit unions as modern financial intermediaries, especially in terms of overall management skills and delinquency management policies, procedures, and practices. Equally important, opening new forums for exchanging ideas, experiences, and vision is important to stimulate the development of appropriate leadership skills and orientation.

The second major problem is the small resource base of most credit unions. With the exception of a few small seed-capital loans, credit unions in Ukraine depend entirely on savings (shares and deposits) of their members. Because of the economic crisis, these deposits tend to be small, with the result that credit unions are unable to respond to member demand for loans. This inability to meet loan demand, in turn, limits the rate of growth in the credit union. Increasing the capitalization and base of loanable funds for existing credit unions needs to be a priority of any effort to assist credit unions in the country.

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[17] Actual members as a percentage of the total potential number of members in the primary field of membership.

[18] Some observers have commented on the "moral hazard" that accompanies expanding membership beyond the immediate field of membership in which all members know each other personally. Although it is true that having a very limited field of membership reduces credit risk because of peer pressure on borrowers, for credit unions to grow and become significant providers of financial services in a community they need to develop alternative mechanisms for credit risk analysis and risk management.

Credit unions also are plagued by the absence of a standardized chart of accounts and inadequate financial accounting software. Previous attempts to develop software for credit unions have not been successful. Credit unions around the world operate with a similar set of services in similar environments. There must be software readily available that could, with appropriate modification, meet the needs of the Ukrainian credit union movement. Arguments that local needs are unique or that the local movement must be in control of the source code are neither realistic nor accurate, and they prevent the credit union system from obtaining the data processing support it sorely needs.

Finally, there are inadequate structures in the credit union and financial systems to support effective liquidity management. Credit unions are unable to develop adequate relationships with the banking sector to handle mismatches in deposits and loan demand effectively, and no facility exists within the credit union system to easily lend and borrow among credit unions to manage liquidity efficiently.

A program of assistance that supports improvements in overcoming these problems and issues would have a profound impact on the growth potential and future viability of the Ukrainian credit union system.

## UKRAINIAN NATIONAL ASSOCIATION OF SAVINGS AND CREDIT UNIONS

The Ukrainian National Association of Savings and Credit Unions was set up in 1994 to serve and represent the interests of its member credit unions. UNASCU has been a member of WOCCU since the International Credit Union Forum in July 1994. Credit union membership in the national association is voluntary, and approximately one-quarter (95) of all registered credit unions (approximately 400) are currently members.

### STRUCTURE

UNASCU is structured as an association, headed by a Board of Directors elected by delegates from the affiliated credit unions. The Board of Directors is made up of nine members. UNASCU also has a five-member supervisory committee. Members on the Board of Directors and supervisory committee serve for three years, with about one-third of the directors of each turning over each year. Both the board and the supervisory committee meet every three months. None of the members of the board or supervisory committee receives financial compensation.

Daily operations are the responsibility of an appointed President, who is tasked with implementing the policies set by the Board of Directors. The President is an *ex officio* member of the Board of Directors.

UNASCU's daily functions are divided into four departments: (1) legal department, (2) financial analysis center, (3) finance department, and (4) regional policy and development department. A fifth department—the training and methodology center—functions as a separate profit center for tax purposes (see below). Through this structure, UNASCU provides the following services to its members:

- Representation at the national, regional, and local levels;
- Staff and board training;
- Curricula development for new training courses;
- Legal and financial accounting support;
- Analysis of financial data on a quarterly basis;
- Some model documentation (e.g., bylaws, registration forms) and recommendations on loan applications, etc.;
- Simple accounting software;
- Collection and dissemination of statistical data on credit unions;
- Linkages to other credit unions internationally, either through twinning relationships, internships, or conferences; and
- Limited marketing and promotion support.

In addition, three affiliated profit centers are associated with UNASCU. These include FORTRESS Insurance (which provides limited insurance coverage to credit unions), a service center (which provides consulting services for UNASCU members and publishes annual reports and other credit union information), and the training and methodology center. The service center and training center are structured as separate entities to permit charging of fees, although they function as integral departments of UNASCU. FORTRESS is, in fact, a separate for-profit corporation.

UNASCU is currently staffed by seven paid employees. In addition, three staff are employed by an affiliated insurance group, one is employed in the services center, and one staff member is employed by the training center. Some of these staff have overlapping duties and perform duties in more than one of the companies. (See Figure 1 on the following page.)

## FORTRESS INSURANCE

FORTRESS Insurance is a separate company formed in 1995 as a joint venture between CUNA Mutual Insurance Society—a credit union-owned insurance company in the United States—and UNASCU. CUNA Mutual owns 90 percent of FORTRESS, while UNASCU owns 10 percent. CUNA Mutual covers all costs, while profits are distributed according to ownership percentage.

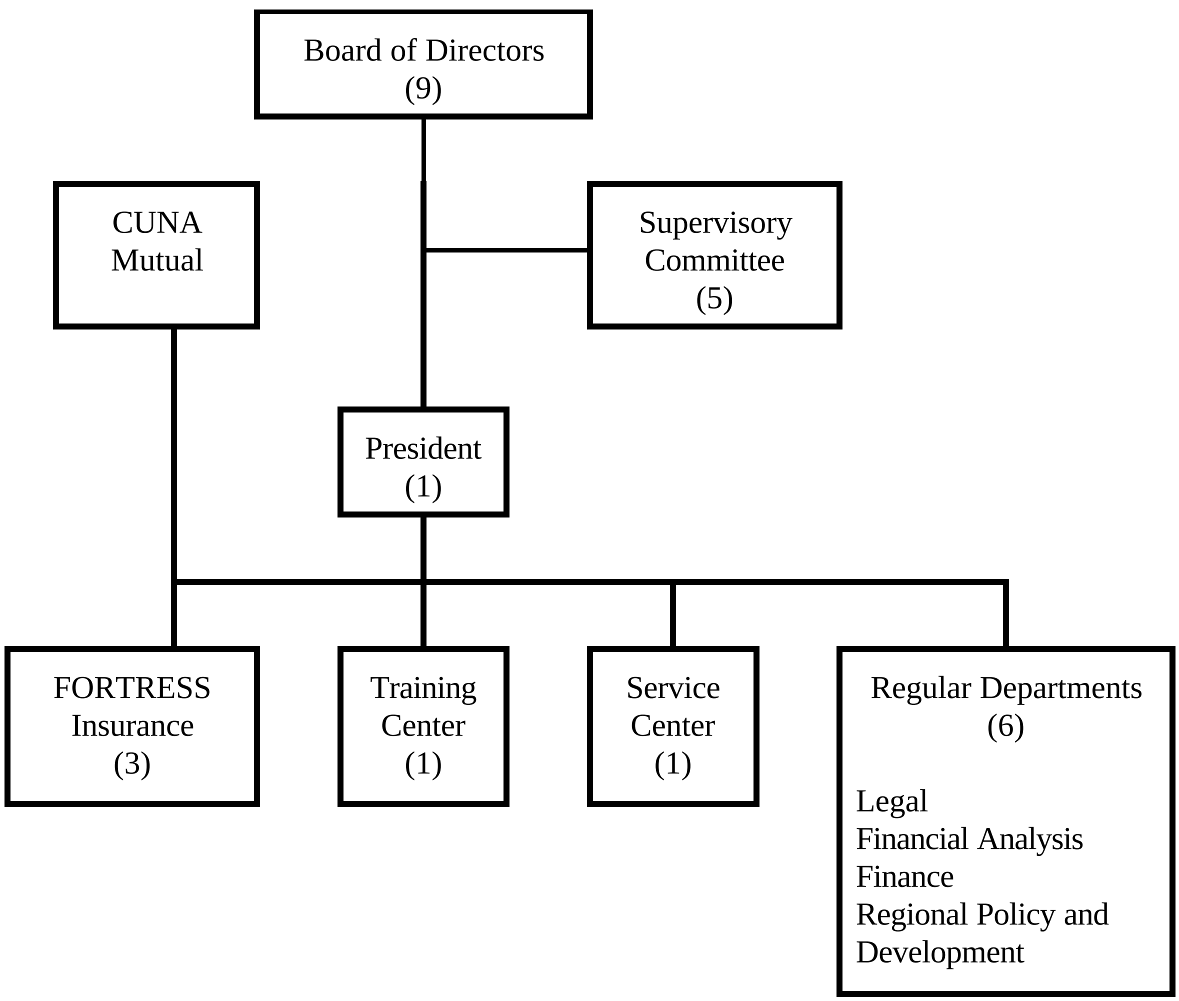
FORTRESS's primary insurance product is loan-protection and life-savings insurance for individual members. If the member dies, the insurance pays off any outstanding loans and provides a 100 percent addition to the member's savings as payment to surviving beneficiaries. This type of insurance—which provides that the "debt dies with the debtor"—has been an marketing tool for credit unions around the world as an incentive for credit union membership.

CUNA Mutual provides other forms of insurance coverage in other countries, but these are subject to extensive risk assessment as well as local laws and regulations. One of the major forms of coverage provided by CUNA Mutual in the United States, for example, is bonding insurance for credit union leaders and staffs—to protect credit unions against fraud or mismanagement. Life insurance for credit union managers to compensate credit unions for the loss of key staff is another important insurance instrument in some countries. CUNA Mutual also provides automobile, life, and other forms of insurance for credit union members. It is likely that some of these additional forms of coverage will evolve as the system matures in Ukraine.

## SERVICE CENTER

The service center is a for-profit entity 100-percent owned by UNASCU. It functions as a department of UNASCU, with UNASCU employees as its staff. It was created as a separate entity because of the tax laws. The primary function of the service center is to provide those consulting services, publishing services and information for which a fee is charged to credit unions that are members of UNASCU. Budget and expense statements are consolidated with those of UNASCU.

**Figure 1**
**Adapted Organization Chart for UNASCU**



## CREDIT UNION TRAINING CENTER

One of the most important departments within UNASCU is the Credit Union Training Center (CUTC), which was established in 1995. Most of the funding for the training center came from the Canadian program and the UNDP. In addition, the center received grants from the Eurasia Foundation in 1997 and from the International Organization for Migration (IOM) to work with the credit unions of the Crimean Tatars. It also received two work orders from the Know How Fund and the International Foundation for Social Adaptation (Soros Foundation) to deliver training courses and to develop training methodologies, curricula, and training materials.

CUTC training courses are available to all members. However, there appear to have been problems in promoting the availability of courses and training opportunities; some credit unions have been well served by the center, while others have been largely unaware of its activities.

As shown in Table 4, the current training curriculum is divided into three levels or modules. A fourth module is being developed.[19] Modules are structured for a variety of credit union staff and board members depending on information and responsibility needs. All management staff and board members are expected to pass beginning modules before advancing to higher levels.

Modules are constantly being updated and refined based on training survey feedback and feedback from credit unions, which also are involved in the curriculum development process. Table 4 provides information on the training modules, the level of participants, and illustrative topics within the modules.

**Table 4**
**Training Modules**

| Module | Level of CU Development | Illustrative Topics |
|---|---|---|
| **Module One** | Newly created and registered credit unions, up to 18 months in age | • How to start and register a credit union<br>• Basic accounting and reporting<br>• The role of boards<br>• Making loans |
| **Module Two** | Credit unions approximately 12 to 18 months into operations | • Attracting deposits and marketing<br>• Psychological aspects of lending |
| **Module Three** | Credit unions in operation 18 months or more, financially stable, but slow growth | • Setting up a branch network<br>• Strategic planning<br>• Personnel management<br>• Business lending |
| **Module Four** *(currently under development)* | Most stable credit unions, looking for new market niches and growth | • Financial projections<br>• Business valuation<br>• Hiring of new personnel<br>• Legal aspects of branch expansion |

[19] Module Four is currently being developed by the CUTC with input from various credit unions in the country.

Before 1998, training was delivered without charge to UNASCU's members. Most of the training went to credit unions affiliated with the Canadian program, in part reflecting the funding sources and in part resulting from the fact that WOCCU did its own training for its 11-model credit unions. Also, in the early years, the center spent significant time and energy disseminating information on credit union standards and "best practices," which was important for the growth of the movement.

Training to credit unions has primarily taken place in Kiev, with 62 of the 126 courses offered between 1995 and 2000 having been held in Kiev. In 1999, more training courses were held in Western Ukraine, reflecting the closer relationship between the CCA program and UNASCU (see Table 5).

The center's training strategy has changed in the last year because of the new regional presence of consultants/trainers financed by the Canadian program. Module One training courses are now being provided by regional consultants of the Canadian program, while the center provides the training courses on the other modules. The center concentrates on following up Module One training with other types of interventions, including:

- Consulting seminars;
- Distance learning (self-training, with a follow-up test conducted by the regional consultants);
- Internships in model credit unions;[20]
- Short courses delivered in the individual credit unions; and
- Practice seminars in which, following a training, a group of credit unions comes together to discuss how the training topic applies to their specific credit unions.

The CUTC also has developed a certification program based on the current training modules. The program is based on a series of tests that credit union staff would be required to complete and pass. Completion of the certification program would allow credit unions to become eligible for such things as a future stabilization fund. It also would create higher standards for the industry.

In addition to training, the training center is providing one-on-one consulting services and other post-training "best practice" reinforcement activities. As with the other training center programs, this not done on a cost recoverable basis.

The UNDP provided a total of $166,030 to UNASCU for operating the training center. This funding ended in December 1999. The CUTC still receives some funding from CIDA. The CUTC has initiated a policy of charging a modest fee for materials and training. Over time, these charges should gradually be increased to cover a greater percentage of the cost of training.

[20] The model credit unions are those models of the Canadian program.

**Table 5**
**Summary of UNASCU Training Courses and Participation**

| Region | 1995 | 1996 | 1997 | 1998 | 1999 | 2000 | Total |
|---|---|---|---|---|---|---|---|
| **Training Courses** | | | | | | | |
| South | 0 | 1 | 4 | 3 | 4 | 0 | 12 |
| East | 0 | 0 | 4 | 1 | 4 | 1 | 10 |
| West | 1 | 2 | 6 | 3 | 22 | 8 | 42 |
| Central* | 8 | 17 | 11 | 11 | 13 | 2 | 62* |
| **Total** | **9** | **20** | **25** | **18** | **43** | **11** | **126** |
| **Hours of Training** | | | | | | | |
| South | 0 | 14 | 100 | 86 | 112 | 0 | 312 |
| East | 0 | 0 | 42 | 14 | 106 | 14 | 176 |
| West | 36 | 20 | 200 | 86 | 282 | 158 | 782 |
| Central* | 184 | 498 | 322 | 200 | 304 | 40 | 1,548 |
| **Total** | **220** | **532** | **664** | **386** | **804** | **212** | **2,818** |
| **Persons Trained** | | | | | | | |
| South | 0 | 29 | 39 | 92 | 69 | 0 | 229 |
| East | 0 | 0 | 21 | 23 | 84 | 6 | 134 |
| West | 14 | 119 | 123 | 65 | 308 | 92 | 721 |
| Central* | 128 | 386 | 221 | 171 | 177 | 16 | 1,099 |
| **Total** | **142** | **534** | **404** | **351** | **638** | **114** | **2,183** |

* Includes Kiev City. Source: UNASCU.

## SELF-SUFFICIENCY

UNASCU, unlike the individual credit unions, is not self-sufficient and is unlikely to become self-sufficient in the near term. This is due to a variety of factors, including the small size and limited resources of the member credit unions and the need for UNASCU to increase services at a time when the movement cannot afford to pay for the level of services needed. One of the paradoxes faced by most young credit union national organizations is that they need to provide a high level of support and services when the membership and asset base of the movements are quite small and the custom of paying for services is not yet developed. Donor support, therefore, is needed in the early years. One of the problems that often affects credit union movements is that the support base often does not develop adequately to sustain the services that have been developed through donor financing.

Likewise, the CUTC is not sustainable at present and is unlikely to become so in the near term. In 1998, the CUTC instituted a new pricing policy for training courses in which part of the costs were covered by participants. However, the costs of the course are still not fully covered by fees paid by participants, despite yet another raise in price in January 2000. The training center director recognizes that the center is not sustainable but thinks the center could become sustainable in two years depending on improved economic stability in Ukraine and the passage of appropriate credit union legislation. Currently, the training center cannot be sustained by such a small movement. Training is extremely important to developing the movement, however, which means that donor support of the training center is needed during the next few years.

Table 6 shows the expenditure budgets and sources of funding for UNASCU for 1999 and 2000.[21] These figures include expenses for the training center and service center. As can be seen, UNASCU depends on donations to cover 80 percent of its current expenses. Furthermore, UNASCU estimates that it needs to nearly double its operating budget to provide the level of services required by its membership. Generating revenues to cover this level of service is a major challenge for the organization.

**Table 6**
**UNASCU Expenses and Sources of Funding, in Hryvna**

| Year | Expense Budget | Source of Funding | | |
|---|---|---|---|---|
| | | Dues | Fee Income | Donors |
| 1999 | 60,074 | 5,197 | 3,960 | 50,917 |
| 2000 | 74,834 | 9,600 | 9,000 | 56,234 |
| Optimal Budget for 2001 | 140,000 | | | |

UNASCU's dues structure is provided in Table 7. To date, most UNASCU services are free of charge and are not covered by member dues. Total member dues paid in 1999 amounted to UAH 20,000. Even if UNASCU were to charge dues at the maximum level of 200 UAH per quarter to all credit unions, it still would raise only UAH 76,000 per year in dues, far below the amount needed to cover its operating expenses.

## INTEGRATION OF CANADIAN CONSULTANTS

Since the WOCCU activity ended in late 1999, the Canadian program has aligned itself more closely with UNASCU. CCA agreed to and is now paying for 25 new regional consultants working throughout Ukraine. These consultants have come from CCA model credit unions and are providing direct, on-site technical assistance to credit unions and conducting Module One training courses for new credit unions. In addition to the training, they provide other follow-up interventions, facilitate consulting from UNASCU, and promote credit union development. Identified as a service of UNASCU, these consultants contribute to developing a positive image of the organization among credit unions.

UNASCU's management and board are well aware of their dependence on donor financing. At the annual meeting in May, the chairman's speech reflected this awareness as he challenged members to consider full sustainability in the near future. In the short run, however, donor funding is required to permit UNASCU to offer sufficient services to provide value to their member credit unions, develop the "branding" necessary to promote affiliation, and earn member loyalty.

[21]Information provided by UNASCU.

**Table 7**
**Dues Structure for UNASCU**[22]

| Credit Union Size | Quarterly Dues |
|---|---|
| Total assets less than 10,000 UAH | 15 UAH |
| Total assets between 11,000 and 100,000 UAH | 50 UAH |
| Total assets between 101,000 and 200,000 UAH | 100 UAH |
| Total assets greater than 200,000 UAH | 200 UAH |

## MAJOR PROBLEMS

As a young organization with extremely limited resources, UNASCU faces a number of immediate problems. It has an incomplete package of services, in that it lacks many of the services that a member-based association needs to be able to provide to its member credit unions. Because member loyalty will ultimately depend on the value of UNASCU services, UNASCU must develop the ability to offer meaningful services to its members.

Consistent with the lack of service, UNASCU lacks outreach. It has a limited staff and a limited ability to maintain contact in the field with its members. UNASCU needs to develop the ability to maintain a visible presence in the field, providing contacts and services with member credit unions. The consultants provided by the CCA project help extend UNASCU's outreach and help further this visible presence in the field.

UNASCU has an insufficient base of credit unions on which to build a viable national organization—both in terms of numbers of credit unions and the financial size and strength of the credit unions that are members. The movement itself needs to grow to a critical mass of strong credit unions to support a strong national association. This growth needs to take place both in terms of the numbers of credit unions, and in the internal growth and strengthening of existing credit unions.

Because of its small membership base, limited range of services, and recent creation, UNASCU is unable to support itself on self-generated income. Instead, it has to depend on external donors, making it vulnerable to changing donor interests and priorities. Growth in the movement will be gradual, so UNASCU needs to find a balance between dependence on donor funds and financial stability as it develops a portfolio of services and the staff to deliver services to its members.

Based on conversations with credit union leaders around the country, it appears that, despite strong support for UNASCU, there is insufficient involvement of members in UNASCU activities and decisions and a feeling that UNASCU is not adequately responsive to its members. In

[22]The dues structure for UNASCU was established when the exchange rate was 1.8 UAH to the dollar. Currently, the exchange rate is hovering around 5.4 to the dollar. The Board of Directors is responsible for changing the dues structure. It was not changed at the annual meeting on May 26, 2000. Source: UNASCU.

particular, UNASCU needs to able to respond to and promote the growth of its larger members. As mentioned earlier, 14 credit unions account for 60 percent of the assets in the affiliated movement. Even though the largest of these has only US$136,000 in assets, which is small by international standards, these credit unions will quickly develop a sophistication that will threaten their affiliation with UNASCU if the latter cannot develop a level of services that responds to their needs.

Finally, UNASCU needs to grow as a membership-oriented association. It needs to find additional ways to involve its members in discussions, strategy development, sharing of ideas, and decision making. It is this democratic aspect of the credit union system that ultimately determines its strength and cohesion.

## SUMMARY

The credit union system in Ukraine is young, small, and financially weak. Nevertheless, it has attracted more than 60,000 members and mobilized nearly US$2 million in member-owned savings. With continued growth and improved performance, the credit union system could grow to play an important role in the provision of financial services to the middle and lower classes.

# CURRENT ENVIRONMENT FOR CREDIT UNIONS IN UKRAINE

The credit union movement in the Ukraine exists in a transitional economic, political, and social environment that profoundly affects the stability, growth, and eventual success of the movement. The current status of the credit union system reflects the instability and changes in these environments.

## CURRENT ECONOMIC SITUATION

Like other countries in Central and Eastern Europe, Ukraine faces the challenges of transitioning from Soviet times into a market economy under democratic rule. Sharing its largest border with Russia and with its economy so intricately tied to Russia's, the challenges of transitioning to privatization and democracy are understandably pronounced and prolonged.

Ukraine continues to experience a severe economic contraction that was brought on by the collapse of the economic system that has been in place during the last 55 years and the sudden economic crisis precipitated by the Russian financial crisis of 1998. This contraction has resulted in increased unemployment, decreased wages, and a substantial drop in the standard of living for most Ukrainians.

At the time of the mid-term evaluation of the WOCCU project in February 1998, the macroeconomic environment of Ukraine had improved significantly since project start-up in September 1995. Annual inflation was between 10 and 20 percent, and in early 1998 the year-end forecast for inflation was 18 percent. Six months later, in August 1998, the effects of the Russian crisis reached Ukraine, which now faced its own financial crisis. By year-end 1998, inflation had reached an annual rate of 105.7 percent and the hryvna had been devalued by 55 percent, from UAH 1.89 per U.S. dollar at the end of 1997 to UAH 4.32 per U.S. dollar at the end of 1998.[23]

As a result of the difficult economic situation, members and potential members of credit unions find it more difficult to save and are less able to manage debt, which will keep the natural growth of credit unions relatively slow. Credit unions underwent a net loss of real assets, deposits, and value of loans in the 1997 to 1998 period because of the economic crisis. Growth has gradually returned to the movement, but at a slower pace.

At the same time, however, these conditions provide a natural environment for the success of credit unions. They are precisely the conditions that gave rise to strong credit union movements in Germany in the late 1800s and in the United States during the Great Depression. These are the conditions in which credit unions—even small, new credit unions—can provide extremely

[23]WOCCU, *Ukraine Project Evaluation*, Draft, May 31, 1999, p. 4.

valuable services to their members that cannot be obtained from other sources, since banks are even more likely to disdain small savings and are more unwilling to grant small loans.

## LEGAL ENVIRONMENT

Credit unions need to operate in the context of an unambiguous legal framework. At present, credit unions in Ukraine operate under a presidential decree, promulgated in September 1993, that granted credit unions the right to form, described the basic structure of a credit union, and permitted them to accept deposits from and extend loans to individuals.

Despite intensive Ukrainian credit union movement efforts, a permanent legal basis for credit unions has not been enacted. By its very nature, the temporary decree of 1993 that allowed the legal registration of credit unions does not provide the comprehensive legislative framework required to operate a modern financial institution and continues to be inadequate for credit union formation and operations. The current presidential decree permits credit union operations, but many aspects of credit union status and operations are unclear or inadequately defined—especially in terms of credit union powers (ability to loan to and borrow from other credit unions and to invest in the credit union structure), services (the definitions of “shares” and “share savings”), and internal legal structure (exactly what constitutes a credit union and what constitutes an investment club or pyramid scheme). In this environment, many “pseudo” credit unions have been formed; failures in these “pseudo” credit unions could have an extremely deleterious impact on the reputation of the entire credit union movement. Furthermore, the implementation and enforcement of current legislation vary from region to region.

Both an adequate legal framework and government supervision and regulation of credit unions need to be in place for the movement to grow and become important actors in the financial services market in Ukraine.

Similarly, although the decree now states that credit unions are non-profit institutions, it does not adequately define the tax status of specific credit union services and operations (“shares”), resulting in an ambiguous application of tax policies by local authorities. Credit unions are operating under a taxation regime that requires them to withhold taxes at a rate of 20 percent on dividends paid on their share accounts—the primary form of savings in young credit unions. This discourages the public from keeping their savings in credit unions since banks are not currently required to similarly withhold taxes on interest earned by clients in their savings accounts.

The current legal framework also does not provide for regulation or supervision of credit union activities by a governmental authority that can set standards, enforce compliance, and oversee the viability and soundness of credit unions in the system.

Finally, the judicial system is weak, internally inconsistent, and ineffective. The decree and other laws are interpreted arbitrarily and applied differently throughout the country. Credit unions seeking recourse in the courts for collecting bad debts are frequently unable to obtain enforcement of court decisions in their favor. Court decisions are further complicated by the *propiska* system, which places restrictions on selling property placed as collateral on a bad debt.

The Ukrainian government and the NBU have been actively working to improve the system, particularly since the Russian financial crisis in late 1998. Several recent and proposed improvements in financial sector legislation, supervision, and regulation will strengthen the overall banking system and have an impact on credit union operations. Recent improvements include the following:

- Starting in January 1998, banks were required to transfer to international accounting standards (IAS), which has increased transparency in financial reporting. Likewise, in January 2000, all enterprises were required to adhere to IAS for all financial reporting. For banks, this is a positive turn because they now have more reliable information upon which to base lending decisions.
- In January 1999, a presidential decree was issued "On Comprehensive Measures to Rehabilitate the Banking System in 1999-2000" that laid out an ambitious plan to further develop the banking sector in accordance with the Basle standards. These measures included a strengthening of capital adequacy standards to the Basle measure, an improvement in bank licensing procedures, and an improvement in the NBU's regulatory authority. This decree is considered "a good start" to passage of a more comprehensive law "On Banks and Banking."
- A centralized registry for the reliable storage of information regarding secured moveable assets became operational in March 1999. By the end of 1999, it had more than 40,000 entries and has allowed for increased lending to commercial enterprises, particularly smaller ones. Passage of a new land code will allow for significantly increased lending as it will remove uncertainty regarding land ownership and will allow the asset to be put to use.
- In general, the NBU has improved its ability to prudentially regulate and supervise banks through periodic reporting, reviews of those reports and on-site examinations.

The Verkhovna Rada is expected to pass a new law "On Banks and Banking" in the near future. This law should address other banking system weaknesses including:

- NBU authority to require that grossly negligent managers and dishonest bank owners reimburse depositors for losses in the case of bank failure;
- NBU authority to liquidate banks (bolstered by appropriate bankruptcy laws);
- "Fit and proper" integrity requirements for managers and large shareholders of banks vis-à-vis their fiduciary responsibilities;
- Strengthened provisions against providing preferential treatment to bank insiders;
- NBU authority to impose corrective orders ("cease and desist") orders on insolvent banks; and
- Stricter enforcement of licensing requirements.

It is anticipated that a new civil code also will be passed by the Verkhovna Rada in the near future. This law could have major implications for credit unions, once and for all allowing for the existence of not-for-profit institutions with a tax-exempt status.

Finally, a draft law on credit unions that would solidify and expand on the provisions of the decree has been under consideration for some time. It passed an initial reading in the Verkhovna Rada, but it needs to pass further readings and be ratified. Top officials in the executive branch of government are supportive of credit unions and the new law, but attitudes ranging from apathy to outright opposition in the Rada have delayed final adoption of the proposed legislation.

Creating a legal framework that supports and protects credit union operations is clearly one of the most pressing needs of the Ukrainian credit union system. The legal framework needs to provide clear definitions of credit unions and activities, clarify tax status, improve the functioning of the judicial system, and provide for prudent regulation and supervision of credit unions as financial intermediaries.

## SELF-REGULATION

In the absence of governmental regulation, the safety and soundness of credit unions depend on self-regulation. In the absence of governmental regulation and supervision, self-regulation is a necessary interim step to ensure safety and soundness. Even when governmental regulations and supervision are in place, self-regulation is needed to provide members with mechanisms for exercising their ownership control and effecting a proactive monitoring of credit union performance. Credit unions have several built-in mechanisms for self-regulation, including:

- The ownership structure, in which the members are the owners with a vested interest in the success of the credit union;
- The democratic structure of the credit unions, in which members vote on officials and select the board of directors and membership committees to monitor the key elements of the credit union, including credit approval and supervision of credit union performance;
- An established body of polices and procedures, embodied in bylaws (internal statutes), that prescribe the responsibilities, functions, and operations of the credit union;
- A set of tools (PEARLS, CAMEL, KAPER, DZERKALO and BOKS) to assess and report on credit union performance; and
- Open disclosure of financial records and results to the membership in annual meetings.

This self-regulation is working reasonably well, although the safeguards have not yet matured. In many credit unions, the chairman of the board and executive director are the same person, a concentration of power that can thwart self-regulatory mechanisms. Many of the boards and committees are uncertain of their roles and are not yet carrying out these roles effectively. Members are not fully convinced that they are the owners of the credit unions and are responsible for asserting that ownership control. Still, these mechanisms are in place, and they are functioning reasonably well for such a young movement in an environment that has little experience with member-owned institutions. Any future activities to support credit union development in Ukraine should reinforce and strengthen these mechanisms for self-regulation.

## COMPETITION AND MARKET NICHE

At present, credit unions occupy a unique niche in the provision of financial services in Ukraine. This niche is providing financial services to average citizens (natural persons), both in urban areas as well as in rural communities where a credit union might be located. These financial services include consumer and other types of personal lending, as well as small-scale enterprise and agricultural lending. Credit unions also provide specialized deposit services for short- and potentially long-term savers.

In other countries, credit unions tend to compete with banks; in some places, microfinance institutions to serve this population. However, in Ukraine, banks largely work with “legal entities,” which tend to be large enterprises. Ukrainian banks tend to provide loans to larger enterprises, while credit unions tend to lend for the purchase of consumer goods, education, health care, special occasions (e.g., weddings, funerals), and emergency and short-term loans for member wage arrears. Loans outstanding average UAH 150 (US$27) per member, reflecting the small average loan size made by credit unions, and the majority of loans are disbursed in cash. About half of the credit unions the team visited were building their capacity in consumer lending. Many had already formed alliances with department and appliance stores in their town or region that provide discounts on new household goods to credit union members.

In Ukraine, credit unions also engage in micro and small enterprise lending and agricultural lending—both sectors that are largely unserved by the Ukrainian banks, or by donor-financed microfinance or rural finance institutions. This could conceivably change in the future. The bulk of credit union lending is uncollateralized in the traditional sense, whereas banks require between 100 and 200 percent of the value of the loan in collateral.

On the deposit side, credit unions are beginning to develop a market niche for personal savings. Although deposits in any financial institution are low, members increasingly trust their savings to the credit unions to which they belong. UNASCU member credit unions saw an 87 percent growth in deposits between January 1998 to January 2000. On average, credit unions are paying between 20 percent and 60 percent annually on hryvna deposits, compared to 16 to 40 percent paid by commercial banks.[24] Ukrainian banks also tend to be less interested in small deposits, requiring their depositors to deposit in sums more than UAH 500 (approximately US$92). More important, credit union pay interest monthly and promptly, something some banks do not yet do. In most cases, credit union members have easy access to their deposits. In addition, most of the credit unions visited by the team seemed to understand the risks associated with having a few large depositors. Many institutions were no longer relying heavily on large depositors for their asset base, an issue several years ago.

[24]Information provided on the following website in Russian: www.ifs.kiev.ua/freeinfo/dfr.shtm.

At present, the majority of banks are not interested in entering this low-end market. Loans to this market are seen as too risky and too costly to make given their size, and small savings are not a high priority. A couple of banks in the Lviv area are beginning to engage in consumer lending, but this type of financial service is offered by the banks in other cities and regions. Credit unions also are not competing with microfinance institutions; such organizations are very limited because of legal and regulatory issues related to lending in Ukraine. Thus, many are spending extra energy to learn and institutionalize the methodologies to lend to microenterprises.

## PERCEPTIONS OF CREDIT UNIONS

At present, the general public is largely unaware of the credit union movement in Ukraine. Until recently, there was little or no promotion of credit unions at either the national or local level. UNASCU, the national association that represents the credit union movement in Ukraine, has done limited promotion and has focused its lobbying efforts more on the government than on the Rada. This needs to change. Locally, individual credit unions are just beginning to publicize their activities to their communities to increase membership, but this has been limited because they fear growing too quickly and placing loans with risky clients. Members of credit unions tend to be well aware of their credit union's activities and have a high level of participation in annual board meetings.

The USAID-supported Ukraine Market Reform Education Project (UMREP) has begun a publicity campaign on behalf of credit unions in the past eight months. In the beginning, this campaign targeted journalists through press clubs in 12 regions of Ukraine. In addition, UMREP has sponsored regularly aired radio infomercials on the topic, and has produced a 25-minute film on the Ukrainian and Polish credit union movements. Most important, it has provided training to UNASCU and credit union staff on how to promote credit unions through mass media and how to get information to local people on differentiating credit unions from pyramid schemes. Finally, UMREP, in conjunction with the Canadian program, recently published and distributed 10,000 copies of a glossy brochure on credit unions—what they are and how they function—throughout Ukraine. UMREP has been able to gauge its impact through increased phone calls to their hotlines on credit unions; it received 230 calls in April on the topic, the majority of them from Kiev, Chernivtsi, Vinnitsa, and Lviv oblasts. Frequently asked questions appear in the box on the next page.

**Most Frequently Asked Questions about Credit Unions**

- What is a credit union?
- How does one start a credit union?
- How does one become a member of a credit union?
- What documents are required for credit union registration?
- What is the required number of founders of a credit union?
- What is the rate of an admission membership fee for a credit union?
- Is it legal for a credit union to accept charity donations?
- Who approves the statutes of a credit union?
- Is it legal to coordinate statutory provisions of a credit union with the National Bank of Ukraine?
- What are the credit rates charged by a credit union?
- Is a credit union a not-for-profit organization?
- Are there any credit unions in Kiev?

## SUMMARY

The credit union movement in the Ukraine exists in a transitional economic, political, and social environment that profoundly affects the stability, growth, and eventual success of the movement. The current status of the credit union system reflects the instability and changes in these environments. Sometimes the environment has both positive and negative impacts.

In particular, the difficult economic climate depresses credit union growth by limiting the amount of savings members can deposit and the amounts of loans they can prudently handle. At the same, however, credit unions have historically thrived in difficult economic times because they become one of the few institutions willing to serve the financial needs of individuals.

At the moment, the competitive environment favors credit union growth. Banks are not active in the financial markets that credit unions are entering, and other forms of financial intermediaries do not exist. This could be a temporary situation. If microfinance institutions become established in Ukraine, or if banks become interested in consumer loans and deposits, credit unions could face increasing competition.

The legal environment needs improving, as the law on credit unions has not yet been enacted. This has resulted in an ambiguous legal status that has been subject to arbitrary interpretations by various governmental agencies. Also, credit unions currently lack an authoritative supervisory and regulatory agency.

Finally, the public's awareness of credit unions is slight at the moment. Growth will require building a greater awareness of credit unions among the general public.

# ASSISTANCE TO THE UKRAINIAN CREDIT UNION MOVEMENT

In addition to USAID/Kiev, other bilateral, multilateral, and private donors have supported the credit union movement. The two largest programs of assistance to credit unions have been the USAID/Kiev activities and those sponsored by the Government of Canada.

## DONOR PROGRAMS

### CANADIAN ASSISTANCE TO CREDIT UNION DEVELOPMENT

The Canadian Government, through the Canadian International Development Agency (CIDA), provided two grants to the CCA to finance projects supporting Ukrainian credit union development. An initial grant of 1.4 million Canadian dollars (about US$1.0 million) helped promote initial credit union formation in Western Ukraine from 1993 to 1996. The second of the two Canadian grants was for 4.0 million Canadian dollars (about US$2.5 million) and is funding the Ukraine Credit Union Development Assistance Program. This is a joint project of the CCA and the Council of Ukrainian Credit Unions of Canada that is now in its fourth and final year.

According to the CCA project description, the goal of the first phase of this program was to establish as many credit unions as possible, while the goal of the second phase was to improve the profitability of existing credit unions. Activities under this grant will end in March 2001, and a third phase of assistance is currently being prepared.

CCA states that 102 credit unions have been established with its assistance. Eighteen of these are model credit unions that are obligated to provide technical support to newly established credit unions and to help establish additional credit unions in their respective cities. Many of the participating credit unions have established close relations with UNASCU. Currently, CCA and UNASCU cooperate in the legal and social development of credit unions.

### UNITED NATIONS DEVELOPMENT PROGRAMME

From 1995 to 1999, the United Nations Development Programme provided a grant of US$166,030 to the CUTC, an affiliate organization of UNASCU. The grant went to support the establishment of a comprehensive system for training specialists, providing methodological support and providing consulting services in all spheres of credit union activities. As a result of the grant, thousands of credit union staff, board members, and managers received training throughout Ukraine and the CUTC have been able to develop enough capacity to move forward with new activities including a certification program for UNASCU-affiliated credit unions.

## INTERNATIONAL ORGANIZATION FOR MIGRATION

Working closely with the UNDP Crimean Integration and Development Program, the IOM assisted on the development of a system of credit unions for Crimean Tatars and on training programs for management and staff of these credit unions.

## SOROS FOUNDATION

The Soros Foundation, through its local affiliate, the International Foundation for Social Adaptation, is providing no-interest loans for up to three years to credit unions meeting a selection criteria. The program began working with a Soros program to retrain former members of the military but, in the last year, it has expanded to work with all credit unions. To receive loans, institutions must have:

- Delinquency up to 180 days of less than 10 percent;
- Income/expense ratio of greater than one;
- Reserves to cover delinquency between 30 and 180 days;
- Liquidity ratio (cash on hand plus in banks/total assets) of at least 10 percent; and
- Asset/liability ratio greater than 1.2.

To date, the foundation is working with 15 credit unions. Loans are not pegged to a dollar exchange rate. An additional US$200,000 is proposed for this program. The Soros Foundation also has provided some funding for UNASCU's training center.

Although development purists will argue that interest-free loans to credit unions distort interest rates and interfere with financial intermediation, there are two factors that mitigate the problems associated with "free" money in this situation. First, no interest is charged because only a few selected types of institutions (including banks and credit unions) are allowed to charge interest on loans under Ukrainian law. As a nongovernmental organization, the International Foundation for Social Adaptation may not legally charge interest on money it lends. Second, the amounts are very small and are clearly tied to performance.

The International Foundation for Social Adaptation has documented the impact of even small amounts of grant funding on credit union growth—in terms of both capitalization and loan portfolios. This is understandable, because one of the problems small credit unions have is in providing a sufficient amount of loans to keep members interested and committed to supporting the credit union. Small amounts of loans or grants can, in this situation, stimulate a more rapid growth in credit union members and savings.

**OTHER USAID/KIEV PROGRAMS**

USAID/Kiev has provided other support to the credit union movement through directed support for specific initiatives, such as agricultural lending, microenterprise lending to women, and public education of economic reform activities. These include the extension of agricultural credit through the Ukraine Agricultural Finance Development Foundation, extension of microenterprise loans to women through the Women's Economic Empowerment Project, and public education and promotion of credit unions through the Ukraine Market Reform Education Project. A brief description is provided below:

> *The Ukraine Agriculture Finance Development Foundation* (UAFDF) in Lviv was set up originally to handle funds from the monetization of soybean meal, approximately US$4.0 million, to establish a back-up fund to regular commercial credit provided to private farmers in Lviv and Western Ukraine. The back-up fund was to support projects developed by Land O'Lakes in the dairy sector that would strengthen linkages between Ukraine and Poland. The objective changed over time because of the delay in getting proceeds from the monetization. The new objective became to provide institutional training to credit unions and commercial banks for agricultural lending. UAFDF is now functional and is focusing on financial support to lenders for loans to agricultural and women's business projects.
>
> Among the numerous activities of the *Women's Economic Empowerment Project* is a grant facility to provide five women's credit unions with grants of US$25,000 to provide loans to women microentrepreneurs. The project is providing extensive training to the credit unions on microenterprise lending and on the special needs to women-owned businesses before funding is obligated. To date, credit unions have completed only some of the initial training; none have made any loans yet using this money.
>
> As part of its work to promote public awareness and support for the transition from a command to a free-market economy, the *Ukraine Market Reform Education Project* works to foster an enabling business environment that is secure, transparent, and hospitable to domestic and foreign investment. UMREP uses local media to promote these ends. For the past eight months, it has added credit unions and the valuable financial services they provide at the community level to its promotion agenda.

## MAJOR DIFFERENCES BETWEEN THE WOCCU AND CCA APPROACHES TO CU DEVELOPMENT

Although the Canadian and U.S. programs to assist credit union development in the Ukraine were the two major programs, and overlapped in time, there were significant differences between the two programs. Table 8 is not intended as a comprehensive evaluation or comparison of the two programs. Instead, it highlights some of the major differences in the programs that appear to have had an impact on their effectiveness and accomplishments.

**Table 8**
**Major Differences between U.S. and Canadian Projects**

| | USAID-Kiev/WOCCU | CIDA/CCA |
|---|---|---|
| Budget | Small program of $1 million for three (extended to four) years—about $250,000 per year. | Larger program of $2.5 million over a four-year period, or about $625,000 per year. |
| Relationship with UNASCU | Supported UNASCU in early period, but friction between project manager and Chief Executive of UNASCU prompted a split. | Began to work separate from UNASCU, although CCA always encouraged credit unions to affiliate with UNASCU. After end of USAID/WOCCU activity, CCA activities became much more integrated with UNASCU. |
| Chief of Party | Young, local professional with no previous credit union or development experience. Competed with Chief Executive of UNASCU for position. | Young Canadian-Ukrainian with development experience, although no prior credit union experience. Was not perceived as a competitor for the position of Chief Executive, and could act as a neutral advisor. |
| Focus of Activities | Developed a limited number of strong credit union by focusing on internal financial management and contraction rather than growth. | Focused on promoting the establishment of new credit unions. Used incentive system and provided limited capitalization to encourage formation of new credit unions. |
| Participant Training | Abandoned participant training as too costly. Some twinning occurred, but mostly not sponsored by the project. | Provided extensive participant training through twinning relationships with Canadian credit unions. |
| Use of Grants or Quasi-Grants to Develop Loan Portfolios | Not used. | Small "loans" were made to credit unions; interest due to CCA was used by the credit unions to either sponsor a new credit union or pay for technical assistance. |
| Numbers and Location of Staff | Seven local-hire staff members, all located in Kiev. | Fifteen regular staff members. Main office in Kiev, but secondary office in Lviv. Later hired an additional 25 local credit union people throughout the country as "consultants" to promote expansion of credit union system and help guide the local credit unions. These consultants are identified as both CCA and UNASCU representatives. |
| Geographic Focus | Individual credit unions dispersed around the country—the 11 credit unions were located in nine different oblasts. | Heavy concentration in Western Ukraine, where many of the Canadian-Ukrainian diaspora originate. |
| Involvement of Ukrainian Diaspora | Ukrainian-American credit unions were largely excluded from the planning, management, and implementation of the project. Ukrainian-American credit union involvement with credit union development in Ukraine has occurred outside of official USAID/WOCCU activity. | Ukrainian-Canadian credit unions were heavily involved in all aspects of the CCA activity. |

It is not really possible to evaluate the performance or accomplishments of the two activities. Separate evaluations of the projects exist and can be consulted if such an assessment is desired. What is important is that the differences do seem related to both the accomplishments and perceptions of the two programs; these differences and their implications for project impact should be kept in mind in planning any new USAID/Kiev activity to support credit union development in Ukraine.

The USAID/WOCCU activity was a paradox in many ways, because the performance targets for the activity were heavily weighted toward growth when the focus of activities was on concentration and contraction rather than growth. It is clear that the personal conflict between the WOCCU chief of party and the chief executive officer of UNASCU was disruptive and contributed to the shortcomings of the program. It also is clear that the involvement of the Ukrainian diaspora contributed significantly to the overall accomplishments of the CCA project, and it could have enhanced the accomplishments of the USAID/WOCCU activity as well. The focus of the USAID/WOCCU activity on safety and soundness at the expense of growth appears to have been misplaced. Safety and soundness is important, there are problems in the credit union movement that need urgent attention, and growth should never be promoted in the absence of a parallel commitment to safety and soundness. At this point, however, it appears that the Ukrainian credit union system needs to grow and expand—to reach a critical mass of credit unions and members—rather than to focus nearly all its attention on safety and soundness.

In noting the differences between the programs, the assessment team concluded that many of the characteristics of the Canadian program led to a highly visible and generally successful project, and that many of these characteristics should be built into any new USAID/Kiev activity. These include:

- A larger activity with a larger budget;
- Greater involvement of U.S.-Ukrainian credit union resources in planning and implementing the activity;
- An expatriate chief of party instead of reliance on a local technical advisor;
- A greater emphasis on growth—both in the formation of new credit unions and in the internal expansion of existing credit unions;
- A clear commitment to strengthening UNASCU and building the national movement; and
- A greater emphasis on exposing credit union and association staff to the experiences of credit unions and credit union associations to help them develop a framework of expectations and goals for the future of the credit union movement in Ukraine.

## SUMMARY

Numerous donors are involved in providing assistance to the Ukrainian credit union movement. Most of these assistance efforts are quite small. The two major programs supporting Ukrainian credit union development have been the Canadian CIDA/CCA project and the USAID/WOCCU activity. Both countries may fund follow-on projects in the future; it is especially important that these two programs coordinate closely. If the World Bank eventually approves its rural lending program through banks and credit unions, this could have a profound impact on the credit union system.

# CONCLUSIONS

The modern credit union movement in Ukraine is young. All credit unions currently operating in the country were formed after the collapse of the Soviet Union, and most are less than four years old. Because the movement is young, both individual credit unions and the movement itself are small. Less than 100 credit unions belong to the national association (UNASCU). These credit unions have approximately 60,000 members and total assets of approximately UAH 10.4 million (US$1.92 million).

In spite of the fact that the credit union movement in Ukraine is young and small, growth has been impressive during the past eight years, especially since growth in credit union assets, capital, and loan portfolios depends almost entirely on member savings and deposits. Donor contributions to capitalization have been very small.

Credit unions have demonstrated that they have found a viable niche in the financial market place. They can play an important role in savings mobilization and meeting the personal loans requirements of a sector of the population that lacks access to financial services and that can make effective use of access to those services. Most important, credit unions have the potential for making a major impact on the financial well-being of a sizeable sector of the country's population, and particularly on the lives of women.

The credit union movement faces a number of problems and constraints, however. It is small and undercapitalized. Leaders and credit union staffs are new to credit unions and to the provision of financial services, and they lack the skills necessary to operate credit unions as modern financial institutions. The movement lacks adequate legislation, supervision, and the structure and facilities to perform the tasks expected of it.

These problems, while real, are amenable to improvement through external support. Success in developing a viable credit union movement will be a major benefit to Ukraine. It is not unreasonable to predict a credit union movement of 300 credit unions, 500,000 members, and assets in excess of US$50.0 million within five years, with proper assistance.

USAID/Kiev should strongly consider future support to developing the credit union movement and system in the Ukraine. Proper support can greatly accelerate growth, solidify the foundation of the credit union system, and create the structures and systems that will be necessary for future expansion and soundness.

# RECOMMENDATIONS: A STRATEGY FOR USAID/KIEV SUPPORT TO UKRAINIAN CREDIT UNIONS

The credit union movement in Ukraine, though young and still small, has reached a level of development that will permit it to survive and grow, even without further donor assistance. However, properly planned and implemented donor assistance can greatly accelerate the growth of credit unions and the credit union system, develop a sound framework for future expansion and impact, and significantly increase the benefits and impact of the credit union system for people of modest economic means in Ukraine.

Given the status and the major problems facing the credit union movement in Ukraine, future assistance provided by USAID/Kiev should focus on four major areas:

- Accelerating the growth of base-level credit unions, both in terms of the number of credit unions and in the size and performance of existing credit unions;
- Improving the performance and sustainability of the national association, UNASCU, so that it offers a range of services and performs activities that are valuable to its membership and improves its role as a democratic organization;
- Developing an adequate legal and regulatory environment for the growth of strong credit unions in the country; and
- Developing an effective structure and appropriate technologies for the functioning of a modern credit union system in Ukraine.

These four items are listed in order of priority, although any program of assistance should involve an integrated approach that addresses all four focus areas. Although developing an adequate legal and regulatory environment is indeed important, and can be viewed as a necessary prerequisite to sound credit union development, it should not be the primary focus of any USAID/Kiev effort or treated as a prerequisite for carrying out activities in the other three focus areas for several reasons. First, the legal and regulatory environment is necessarily a dynamic one that is subject to constant change; there is no single “best” solution and no single measure of success, and efforts and solutions need to be constantly revised. Second, success is difficult to predict; an activity can expend significant resources on changing the legal environment and not see results for years and years. The other aspects of credit union development should not be ignored while waiting for changes in the legislation. Third, although credit union performance ultimately requires an enabling legal and regulatory environment, credit unions can function and grow—at least in the short run—without it. Furthermore, the growth and success of the credit union movement stands a better chance of bringing pressure on the political system far better than any donor-supported activity can.

This assistance should be planned over a four-year period, with the first two years concentrating on building sustainable growth, strengthening UNASCU, working to develop the legal and regulatory framework for credit unions, and resolving, if possible, the data processing problems facing credit unions. The final two years would work on sustaining momentum in sustainable growth and on supporting the implementation of two key pieces of the credit union structure—a central liquidity facility and a stabilization fund.[25]

The recommended approach to supporting credit union development in Ukraine differs from the previous USAID/WOCCU activity and from WOCCU's recent unsolicited proposal in several key ways:

- It focuses primarily on growth within a framework of safety and soundness rather than on safety and soundness at the expense of growth;
- It places greater emphasis on integrating project activities into UNASCU and on building UNASCU's role as a member-owned association;
- It includes funding to aid in the capitalization of new, small credit unions;
- It places greater emphasis on training and, in particular, on participant training and on-site experiences in U.S. or third-country credit unions and associations; and
- It provides a mechanism for ascertaining the feasibility of the proposed liquidity and stabilization funds and, if feasible, for supporting their establishment and capitalization.

## PRIMARY OBJECTIVES

Quantitative and qualitative targets can be established for each of the four major focus areas: accelerating growth and competency, strengthening the national association, securing a favorable legal and regulatory environment, and building key components of the credit union system and technology.

### ACCELERATING GROWTH AND COMPETENCY OF CREDIT UNIONS

The credit union movement in Ukraine has reached a threshold of sustainability, but it needs considerable expansion to have a major impact on the economic well-being of the population and to be a major actor in the provision of financial services in the country.

Building a critical mass of successful credit unions is crucial to the short- to mid-term success and impact of the Ukrainian credit union system. The presence of a large number of successful credit unions is essential for stimulating increased membership, and UNASCU's long-term sustainability

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[25] Assuming that feasibility studies for the central liquidity facility and stabilization fund result in a positive conclusion to develop these systems.

depends on having a large base of stable credit unions. The primary focus of any USAID/Kiev activity should be to help the movement—especially the base-level credit unions—grow.

Any assistance program for credit unions in Ukraine should have stimulating the growth of base-level credit unions as one of its top priorities. Growth needs to take place both in terms of the numbers of credit unions, and in the size and stability of existing credit unions. Such growth will require two separate focuses—one on the establishment and formation of base-level credit unions, and the second on improving the financial viability, sustainability, and performance of established credit unions.[26]

With appropriate USAID and CIDA assistance, it is not unreasonable to target an increase in the number of affiliated credit unions from 95 to 200, and a quadrupling in affiliated membership (from 60,000 to 240,000), assets (from UAH 10.5 million to 40.0 million), loans (from UAH 9.7 million to UAH 37.0 million), and savings (consisting of both shares and deposits, from UAH 9.5 million to 34.0 million) within the next four years. Some of this growth will come from new affiliations of existing credit unions, some will come from the formation of new credit unions, and some will come from the internal growth and strengthening of existing credit unions.

This growth must take place within a framework of safety and soundness, for only if the credit unions are capable of managing growing financial institutions and safeguarding the value of their members' deposits will success be sustainable. By the end of the activity, all credit unions must have good accounting and data processing systems, and they must be using standard techniques for monitoring performance, managing assets and liabilities, and controlling the risks inherent in managing a modern financial institution. All affiliated credits should be within the standards and norms established for safe credit unions.

## IMPROVING THE EFFECTIVENESS OF THE NATIONAL ASSOCIATION

UNASCU faces the paradox of many young national organizations—it needs to provide a broad range of high-quality services at a time when it lacks the resources to provide those services. The objective should be to help UNASCU develop to the stage where it is a fully self-sustainable national association that is offering a full range of needed and valued services to its member credit unions in a democratically controlled structure. By the end of the activity, UNASCU should have:

- Successfully "branded" the national movement, with "Certified Excellency" for credit unions (based on growth, services, and financial soundness), "Certified Credit Union Managers" (based on sound training programs and materials), and other programs that convey value to affiliated credit unions;
- A well-developed set of standards for credit union accounting and performance that are used internally by member credit unions, and an internal

[26]Both focuses do not have to included within a single project. With the emphasis of the CIDA/CCA project on promotion and formation of credit unions, it may be possible to constructively divide the effort so as to avoid unnecessary duplication.

system for monitoring the performance of credit unions, identifying problems, and helping credit unions that need assistance;
- A set of training materials and sustainable methods for delivering that training to ensure the continual upgrading of credit union management and leadership skills;
- Effective outreach to member credit unions through a more regional presence; and
- A democratic structure that effectively mobilizes volunteer leaders in committee structures and decision making nationally.

Furthermore, UNASCU needs to become operationally self-sufficient within a five-year timeframe, and it must demonstrate progress toward that self-sufficiency over the course of the activity. In the course of developing these capabilities, it may need to develop and provide services that will not become a permanent part of its service portfolio. The provision of temporary services needed to build and develop the movement will be the responsibility of the USAID/Kiev grantee, working in close coordination with the UNASCU Board of Directors and senior staff.

## IMPROVING THE LEGAL ENVIRONMENT FOR CREDIT UNION DEVELOPMENT

Securing passage of appropriate credit union legislation and establishing an appropriate regulatory and supervisory process for credit unions is necessarily a high priority of the credit union movement. The objective of any activities to improve the legal environment should be to achieve a favorable legal and regulatory environment that allows credit unions to function as modern financial intermediaries that have the powers to:

- Provide all financial services required by their members;
- Invest in appropriate second-tier credit union institutions (such as liquidity and stabilization funds);
- Lend to and borrow from other financial institutions and second-tier credit union organizations without incurring a tax liability; and
- Declare and distribute dividends without incurring a tax liability.

In addition, credit unions eventually need to be supervised and regulated by a governmental agency that shares a commitment to credit union growth and success within a common framework of safety and soundness.

The proposed credit union legislation that is under consideration in the Verkhovna Rada is a major step forward in securing an appropriate legal and regulatory framework, and securing passage of that law needs to be a major focus for USAID/Kiev assistance. However, it is important to recognize that political bodies make their own decisions and that considerable efforts may be expended in lobbying for legislation without achieving tangible results.

## DEVELOPING CREDIT UNION STRUCTURE AND TECHNOLOGIES

Unlike other financial institutions, credit unions do not compete directly with one another because of their limited fields of membership. Consequently, they are capable of building systems and sharing programs that help them overcome the limits of small size. Several such systems and programs have been identified as potentially valuable to Ukraine's credit unions: a central liquidity facility, a stabilization fund, and a common automated accounting system.

### Liquidity Facility

Ukrainian credit unions need to improve their asset-liability management. As very small institutions, many credit unions are unable to meet seasonal demands for loans or make suitable use of seasonal liquidity. Some credit unions are currently lending to other credit unions, but only in the form of personal loans to executive directors or chairmen of other credit unions. This type of credit union borrowing, which began following the financial crisis in late 1998, is continuing in limited cases between credit unions that have close historical ties.

A central liquidity facility (central credit union) that could allow credit unions to invest excess deposits short term and gain access to short-term loans would be one plausible approach to meeting this need. At this time, however, a liquidity facility or central credit union does not appear to be a viable option to the Ukrainian credit union system. The movement right now is still quite small and distrustful. Also, most credit union managers do not have sufficient skills in asset-liability management to understand the advantages of borrowing at commercial interest rates to meet temporary and seasonal loan demand. Most important, however, the legal framework is too ambiguous. Although a central credit union would address liquidity problems faced by credit unions, the legal framework would first have to change to allow credit unions to invest in such a facility and to engage in credit-union-to-credit-union borrowing and lending to take place.

The options for establishing a central liquidity facility should continue to be explored jointly by donors and UNASCU.

### Stabilization Fund

Credit union failures in the country could seriously undermine public faith in credit unions as safe financial intermediaries. Long before share/deposit insurance was available, U.S. credit unions banded together to establish association-run "stabilization funds" to ensure the protection of member deposits in the event of a failure. These stabilization funds served a vital role in creating an image of stability for credit unions; they were superceded by the establishment of federal deposit insurance.

A stabilization fund into which credit unions would pay a percentage of their total assets could help the Ukrainian credit union system in a similar fashion. However, the base of the credit union system appears to be too small to adequately support such a fund from internal sources. Furthermore, a small credit union movement may not be able to spread risk adequately to operate such a fund. The option of creating a stabilization fund should continue to be explored by the various donors and UNASCU.

### Common, Automated Accounting System

The previous USAID/WOCCU activity included a component to develop a common automated accounting system for the credit union system. For a variety of reasons, this activity did not succeed and was abandoned; the software never functioned properly, and the operating system is now considered obsolete. UNASCU subsequently adopted a local software package in order to provide some support to credit unions needing automation.

Credit unions in many developed and underdeveloped countries face the problem of finding and using appropriate integrated software. Moreover, it can be a costly and time-consuming activity to undertake. The small size of most credit unions in Ukraine may make it difficult to justify large-scale development efforts. Nonetheless, all credit unions with which the team met stressed the need for automated data processing support and expressed difficulties with adapting the currently available software so that it functioned properly. In addition, because this software handles only the accounting side of the business, portfolio management must be handled manually.

A new USAID/Kiev project should continue to explore viable solutions for meeting the data processing needs of the country's credit unions. If possible, the provider of technical services to the new activity should be required to offer a functioning package as part of its in-house capabilities to support the local movement.[27]

### Summary

In summary, three major components of the credit union system structure have been identified as needing immediate attention:

- A central liquidity facility (probably in the form of a central credit union) that can accept short- and long-term deposits from affiliated credit unions and make short-term loans to meet seasonal liquidity needs and other short-term liquidity needs of credit unions;
- A stabilization fund that provides adequate safeguards to member deposits in the event of a credit union failure; and
- A functioning credit union accounting system, based on international accounting standards, supported by readily available computerized data processing that adequately handles loans, deposits, and shares in the context

[27] As in many countries, the Ukrainian credit union movement mistakenly believes that it has unique requirements that can be met only by custom-designed software and that it needs to own the source code to any software package that is used. Part of the process of exploring software options needs to examine these assumptions and develop a broader awareness among credit union (and association) managers and boards about the dangers and limitations of internally developed systems.

of an integrated accounting system, and that provides on-time management information needed for the daily management of a safe and sound institution.

All three of these systems need to be thoroughly studied during the first year of the new activity. At the end of that period, the activity should have produced a definitive recommendation for each of the three systems and a detailed business and implementation plan for each system recommended for implementation.

Quantitative and qualitative performance targets for each system would be established once a decision to implement the system is made.

# ACTIVITIES

## ACCELERATING GROWTH AND COMPETENCY OF CREDIT UNIONS

The credit union system in Ukraine needs to grow for credit unions to become a significant financial intermediary in the country. Credit unions need to serve a larger membership base, and they need to satisfy more of their members' financial needs. Growth in the movement can come from three different sources: formation of new credit unions, growth in existing credit unions, and new affiliations of existing credit unions.

Formation of new credit unions requires building the image of credit unions at the national and local levels; promoting and supporting the formation of new credit unions; developing the management capabilities of new credit union boards, committees, and staffs; assistance with initial capitalization; and other temporary financial assistance. The CIDA/CCA project has done a very good job in promoting the formation of base-level credit unions and, if they choose to do so, should probably continue to handle this function.[28] If the USAID/Kiev grantee becomes involved in new credit union formation, it needs to:

- Promote additional credit unions in traditional strongholds of credit union success—such as key factories, occupational groups, and associations;
- Develop incentives for existing credit unions to sponsor the formation of new credit unions (much as the CCA credit union program does);
- Include basic management, board, and credit union philosophy training for the new credit unions;
- Introduce principles of safety and soundness at the early stages of credit union operations;
- Provide a limited amount (up to UAH 50,000) of matching grant (or loan) funds to accelerate lending operations and build enthusiasm and interest in the credit union; and

[28]However, USAID's UMREP project provides an extremely valuable service in promoting credit unions and developing the ability of credit unions to promote themselves. This function should be continued, and even expanded.

- Provide limited financial support for computerization and accounting systems.

Most of the growth of the system over the next four years needs to come from growth in existing credit unions. At a minimum, all credit unions should triple their membership, assets, savings (including shares and deposits), and loans during the period. This will require:

- Continual support from activities such as those of the UMREP project;
- Development of a vision of growth and commitment to growth among credit union volunteers and staff;
- Development and employment of promotional tools and techniques within the credit unions to increase the visibility of credit unions in their local markets;
- Deepening of the base of management skills in the credit unions, to cover skills in asset-liability management, cost containment, loan promotion, interest rate determination, problem analysis and solution, and strategic planning; and
- Installation and employment of necessary tools and technologies for credit union management and administration—in particular, computerized accounting systems.

Credit union growth among existing credit unions implies, first and foremost, increasing market penetration among the credit unions' primary fields of membership. This requires promoting membership, offering services that meet member needs, and offering stability and safety for member savings and deposits. Beyond the immediate, primary field of membership, credit unions will need to expand their vision of their field of membership. Credit unions in Western countries expanded membership eligibility to family members and children (for limited savings services). They developed the concept of "once a member, always a member" to allow members who leave the primary field of membership to continue to use the services of the credit union.

New affiliations will occur as the need to affiliate increases. As UNASCU becomes more relevant to the growth and survival of credit unions, and as the services it offers become more important and valuable to credit unions, new affiliations of existing credit unions will occur. Successfully "branding" the national movement, with image-enhancing services such as a "Certificate of Excellence" or a "Qualified Credit Union Executive," will enhance the image of credit unions as a sound financial institution. It also can provide a powerful incentive to affiliate because of the marketing power of such a designation. Adding services, such as a central liquidity facility (central credit union) and a stabilization fund, also will provide a powerful incentive for credit unions to affiliate with the national movement.

All growth needs to take place in the context of improving safety and soundness. Methods and techniques for monitoring performance, identifying problems quickly, and taking remedial actions need to be introduced and constantly reinforced in all credit unions so that, by the end of the activity, credit unions routinely monitor and take action on problems.

## IMPROVING EFFECTIVENESS OF THE NATIONAL ASSOCIATION

USAID/Kiev's role in strengthening UNASCU should be to help it:

- Offer, in the short run, expanded services in training, publicity and public relations, marketing, strategic planning, lobbying and representation, and member relations;
- Develop the practice of using volunteer committees to discuss, recommend, and build support on key issues and services;
- Improve and expand on standards, policies, and internal procedures;
- Develop its internal strategic planning capability;
- Expand its regional outreach and presence;
- Resolve the problem of standardized accounting and computerization of credit union operations; and
- Explore the feasibility and develop key elements of the national credit union infrastructure—such as the central liquidity facility and stabilization fund.

One of UNASCU's major threats in the future is that its larger credit unions will outgrow its services.

## IMPROVING THE LEGAL ENVIRONMENT

Securing passage of appropriate credit union legislation and establishing an appropriate regulatory and supervisory process for credit unions are necessarily high priorities of the credit union movement.

Although local personnel can carry out lobbying and representation locally, USAID/Kiev could assist in this process by providing resources to bring short-term experts to consult on the characteristics of proposed laws and regulations and to add "expert" testimony to support the credit union movement's position to national decision makers. USAID/Kiev should include a long-term position for a skilled lobbyist for the first two years of the project to assist in implementing UNASCU's lobbying efforts.

**DEVELOPING THE CREDIT UNION STRUCTURE AND TECHNOLOGIES**

Although it is premature to actually establish either a central liquidity facility (central credit union) or a stabilization fund, such facilities will eventually be required by the movement. These facilities are complex business ventures, and require careful analysis and planning.

USAID/Kiev could assist in this analysis and planning phase by providing short-term technical expertise to work with local experts, credit union volunteer committees, and UNASCU staff. During the first year or two of the proposed activity, short-term experts would provide training and information on the operations of such funds, and they would help in conducting feasibility studies and preparing business plans for consideration by the UNASCU board.

If a decision is made to implement either or both of the capitalization or liquidity funds, USAID/Kiev could provide additional support in terms of:

- Funding to partially capitalize the funds; and
- Longer term technical assistance in establishing the funds, managing the funds initially, training local staff to manage the funds, and developing the internal policies and procedures to operate the funds permanently.

## COMPONENTS OF A PROPOSED FOLLOW-ON USAID/KIEV CREDIT UNION SUPPORT ACTIVITY

USAID/Kiev should strongly consider future support to developing the credit union movement and system in the Ukraine. Proper support can greatly accelerate growth, solidify the foundation of the credit union system, and create the structures and systems that will be necessary for future expansion and soundness. USAID/Kiev support to credit union development would consist of technical assistance, institutional support, training, and, possibly, partial funding for the capitalization of one or more funds.

This assistance should be planned over four years, with the first two years concentrating on building sustainable growth, strengthening UNASCU, developing the legal and regulatory framework for credit unions, and resolving, if possible, the data processing problems facing credit unions. The final two years would work on building momentum in sustainable growth and on supporting the implementation of two key pieces of the credit union structure—a central liquidity facility and a stabilization fund—if feasibility studies confirm the viability of these funds.

A long-term expatriate advisor should lead the activity for the first three years. During the first two years, the advisor would coordinate the work program with USAID/Kiev and UNASCU, plan and coordinate the activities of short-term advisors engaged in specific program development activities, manage the services of local consultants and staff, and assist UNASCU in developing its role as a democratic, member-oriented association. During the third year, the advisor would manage the transition of project-funded staff and activities to UNASCU and supervise the start-up of any activities designed to support the liquidity and stabilization funds. Project activities in the fourth year would be specialized activities related to establishing the liquidity or stabilization funds. These activities would require specialists rather than a generalist team leader.

The following description of the components assumes that the U.S.-funded program is fully responsible for each of the activities. This may change as the programs of other donors, especially CIDA, become more apparent.

## TECHNICAL ASSISTANCE

USAID/Kiev would finance a grant for technical assistance through a non-profit, U.S.-based organization. Technical assistance would consist of:

- A long-term expatriate advisor serving as chief of party to oversee the project; serve as a liaison with USAID/Kiev, UNASCU leadership, and other donors; establish and oversee technical and performance standards during the life of the activity; and coordinate development resources and efforts;
- Short-term expatriate technical advisors as needed for developing and teaching internal operating technologies (such as performance standards and monitoring), developing a strategic planning capability, developing growth strategies and approaches for credit unions, further develop training materials, etc.;
- A core staff of long-term local technical advisors to manage and implement the core subactivities of UNASCU strengthening, training, and performance monitoring;
- Local consultants to work directly with credit unions to assist in implementing growth, safety and soundness, asset-liability management, and other skills and practices; and
- Short-term expatriate advisors to assist in conducting feasibility studies on stabilization, liquidity funds, and data processing. If a stabilization or liquidity facility is established, a long-term advisor would be needed to help in initial management, development of policies and procedures, and training of permanent staff for the facilities.

The long-term advisor/chief of party should be Ukrainian-speaking expatriate advisor with actual experience in a management position in a growth-oriented credit union and experience in a credit union association. Credit union experience is needed to be able to orient the program toward developing a vision of growth and service and for helping credit unions understand how to manage that growth. Credit union association experience is needed to be able to help UNASCU develop into an effective, service- and member-oriented national association. This person would be needed for the first three years of the four-year activity. A draft Scope of Work for the position appears in Appendix C.

Needed short-term technical assistance consists of:

- Credit union and association strategic planning advisor (two person-months per year during the first two years and one person-month per year in the final two years of the activity) to begin a regular, systematic process of strategic growth-oriented planning both in UNASCU and in the larger credit unions—focusing on market niche, competition, market penetration, growth possibilities, and methods for promoting growth;
- Standards and self-regulation specialist (two person-months per year during the first two years and one person-month per year in the final two years of the activity) to further develop and institutionalize the use of performance ratios and standards to proactively manage a credit union and a credit union system;
- Legislative and regulatory specialist (three person-months during the first year) to help further refine and promote the legislative and regulatory agenda in the context of worldwide experience with credit union legislative and regulation;
- Data processing specialist (two person-months during Year 1) to help UNASCU and the credit unions assess options and plan a strategy for meeting the data processing needs of the affiliated credit union movement;
- Stabilization fund specialist (three person-months in Year 1 or 2) to help UNASCU and the credit unions assess the feasibility of establishing a stabilization fund and preparing a business plan for establishing and operating the fund;
- Central credit union specialist (three person-months in Year 1 or 2) to help UNASCU and the credit unions assess the feasibility of establishing a central liquidity facility—probably in the form of a central credit union—and preparing a business plan for establishing and operating the central liquidity facility; and
- Others as needed (estimated three person-months per year).

If the feasibility studies demonstrate the advisability of establishing either (or both) a stabilization fund or a central liquidity facility, long-term advisors to support the establishment of the stabilization and liquidity funds would depend on the results of the feasibility studies and business plans. A preliminary estimate is that one person would be required for six months for each of these funds.

Local technical advisors would work within UNASCU to help implement the key activities of the long- and short-term technical assistance. Four local technical advisors would be required:

- Legislative/regulatory advisor to help UNASCU promote the legislative and regulatory agenda before the Verkhovna Rada. This would be a part-time position of approximately six-months per year during the first two years of the activity.
- Training advisor to help UNASCU's CUTC complete development of its training package, prepare trainers through train-the trainer activities, and

assist in decentralizing and expanding UNASCU's training outreach. This would be full-time person during the first three years of the activity.

- Strategic planning advisor to help UNASCU implement an in-house strategic planning process with its senior staff and board and plan and deliver strategic planning assistance to its larger affiliated credit unions. This would be a full-time position during all four years of the activity.
- Standards and self-regulation advisor to help UNASCU continue to improve its own oversight of affiliated credit unions and implement programs of self-regulation within all affiliated credit unions. This would be a full-time position during all four years of the activity.

Use of local technical advisors would be structured so that UNASCU would absorb these functions over the life of the project—either through hiring the advisors itself or through the training of existing UNASCU staff. If the former, financial assistance for the advisors would be phased out over the final two years of the activity; if the latter, the advisors would be financed by the activity during the four years.

Local consultants would consist of experienced Ukrainian credit union staff members who would work at the local or regional level to assist in extending the outreach of key services—specifically strategic planning, self-regulation, and training. They would be hired temporarily from their credit unions to gain greater in-depth understanding of credit union operations, growth strategies, and self-regulation methodologies to promote these skills and to impart advanced training using UNASCU-developed advanced training materials to credit union staffs and boards. At the end of the activity, some of these consultants would be retained as permanent UNASCU field staff; others would be qualified to manage or serve in other advanced staff positions of credit unions. A minimum of 10 to 12 such local consultants would be required.

Other direct costs of the technical assistance would include office space, supplies and materials, mobilization and transportation, and equipment.

## INSTITUTIONAL STRENGTHENING

In the past, institutional subsidies to the credit union movement, particularly to the national association in other developing countries, have led to significant dependency by the movement on outside funding to support activities. In Latin America, it has been difficult to develop an independent, member-supported national association with the plethora of free donor money. We do not recommend long-term institutional support to the national association for this reason. However, recognizing that the movement is young and small, it cannot currently support a national association that provides needed services at a sufficient level to satisfy the needs of its affiliated credit unions.

Under a new project, USAID/Kiev should therefore consider a two-pronged approach to institutional support. Both approaches are intended to lead UNASCU to long-term self-sufficiency. The first, more traditional approach is providing funding for selected activities on a declining basis, requiring increased UNASCU cost-sharing over time. Generally, these activities increase the strength of a movement through member and asset growth, promote greater democratic participation of credit unions members and leaders, and promote soundness and stability in the medium term. The second approach, a work-order system, originally instituted by the Development of Support Networks to Assist New Small and Medium-Scale Business (NewBizNet) Project for business services provider activities, is a more market-driven approach to getting activities completed on a fee-for-service basis. Both approaches would prepare UNASCU at the beginning of the project for self-sufficiency by project completion. UNASCU's affiliated training center has operated under a similar work-order arrangement with other donors, including Soros and IOM.

### Specific Institutional Strengthening Tasks

Through the institutional support component, USAID/Kiev would provide temporary budget support to selected activities, either on a declining basis with an increased UNASCU cost-share over the life of the project or on a voucher or work-order basis. The purpose of institutional support is to ensure the provision of key services or activities that are either short term in nature or that are essential but cannot yet be covered through self-generated income. This type of support would be provided for the following activities:

- A new UNASCU working committee structure that would increase the democratic participation of more credit unions in UNASCU—funding might be provided for the first year to cover the costs of holding selected committee meetings;
- At least 10 additional regional support consultants for UNASCU for two years (these people, as with the Canadian program, would be on temporary loan from credit unions and would be folded back into the staffs of the credit unions from which they came);
- Curriculum development for the CUTC. A work order or several work orders might be competed among credit unions that are interested in furthering training module, curricula, and materials development;[29]
- Development of the certification program for the CUTC;
- Lobbying activities—a work order might cover the salary and support costs for a local lobbyist to work on or with UNASCU's staff until passage of new legislation; and
- Training of trainers (TOT) for future CUTC specialists. Local institutions might be able to compete for work orders to do the TOT, particularly for newer training modules.

[29]The assessment team met with a number of credit unions whose volunteer staff and managers were actively working on the development of training materials and curricula.

### Small Grants Program

Other donors—including the Canadians and the Soros Foundation—have provided outside capital to credit unions in Ukraine, primarily in the form of no-interest or low-interest loans to assist in building the credit unions at a point when they lack the income to undertake key improvements internally. Two forms of grants programs have been used in Ukraine:

- A small capitalization grant fund to provide grants to newly formed credit unions to accelerate lending operations and build interest in the movement; and
- A grants facility to which new credit unions may apply for equipment, supplies, and assistance with computerization and accounting systems—as the Canadian program has implemented with great success.

Capitalization grants are intended to "jump start" credit union lending and build member confidence in the ability of the credit union to deliver financial services.[30] The assessment team recommends that a new USAID/Kiev project consider providing outside funding in the form of either a performance-based, local currency loan that can convert to a grant over time or a low interest loan.[31] The amount of outside financing per credit union, however, should not exceed the amount of savings mobilized by the institution up to a pre-established limit—such as UAH 25,000 to 50,000—to minimize distortionary effects on savings mobilization. Furthermore, such grants should be made only to those credit unions that are vigorously pursuing sound credit union objectives and procedures. Conditions should be similar to those adopted by the Soros Foundation—a minimum of one year of operations, delinquency rate of less than 10 percent, income/expense ratio greater than one, reserves should cover delinquencies of greater than 30 days according to standard provisioning, liquidity ratio (cash on hand plus in banks/total assets) of at least 10 percent, and an asset/liability ratio greater than 1.2.

Small grants for equipment purchases have been used to help credit unions purchase office furnishings and computer equipment. Safes, supplies, and printed materials also could be supported through a small grants project for new credit unions.

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[30] International experience with outside financing in the credit union movement, however, has been mixed. In Latin America, the Inter-American Development Bank provided credit unions with significant amounts of low interest loans. Credit unions became dependent on these cheap sources of funding and ignored mobilizing savings from their members. As a result, when low-interest money was suddenly withdrawn, credit union systems in Latin American suffered a significant downturn.

[31] Current laws place an onerous tax burden on grants, so the preferred method of providing assistance in the past has been through no-interest loans.

## PARTICIPANT TRAINING ABROAD

Support of continued training of credit union staff, management, and board members is an important ongoing activity. In addition to providing institutional support to the CUTC through work orders and grants, USAID/Kiev should consider supporting international training through participant training internships or study programs in the United States and other countries. USAID/Kiev funds could be leveraged through more effective twinning relationships with foreign credit unions. These types of training have proved to be successful teaching techniques. Almost all credit union leaders who participated in such programs in the past indicated they learned a great deal from the experiences of other countries; actually seeing a successful credit union or association in operation is far more effective than merely reading or hearing about them. Thus, eliminating this form of training may prove to be false economy in the long run.

Because this type of participant training can be costly to implement, the new USAID/Kiev activity should consider building on the relationships already established by credit unions in the United States with those in Ukraine, many centered on a common Ukrainian heritage or on sister city relationships. Training in a neighboring country—such as Poland, where the credit union movement has solved some of the problems currently facing the credit union movement in Ukraine—could be a more cost-effective form of participant training.

At least 10 credit union staff members and 2 association staff members should participate in some form of participant training each year.

## SUPPORT TO DEVELOPMENT OF KEY SYSTEM COMPONENTS

This component would cover the capital costs of developing key components of the overall credit union system. These include initial capitalization of the central liquidity facility (central credit union) and stabilization fund. Also included are funds for purchasing a commercial software package that will serve individual credit unions' needs for data processing support and management reporting.

In all cases, funding for building key system components would be contingent on feasibility studies that show the financial and economic viability of the proposals, and detailed business plans that provide implementation plans, financing arrangements, risk analysis, and cash-flow projections. The first 12 to 18 months of the new activity would be spent on assessing the feasibility of various alternatives for improving liquidity management, stabilization, and accounting/information systems.

After the results of the assessment are known, the new USAID/Kiev activity could support—along with other donors—the implementation of one or more of these alternatives. The liquidity and stabilization facilities would require partial capitalization by the credit unions themselves—typically up to 1 percent of assets. USAID/Kiev funds would be used to provide a margin of coverage above local capitalization capabilities while the credit union system is still small, and would cover the initial risk in these institutions until a strong capital base could be developed.

## DRAFT BUDGET

**Table 9**
**Sample Activity Budget***
(Amounts in US$000)

| Line Item | Year 1 | Year 2 | Year 3 | Year 4 | Total |
|---|---|---|---|---|---|
| **Technical Assistance** | | | | | |
| Long-Term Technical Assistance | | | | | |
| Chief of Party | 200.0 | 200.0 | 200.0 | | 600.0 |
| Local Technical Advisors | 80.0 | 68.0 | 68.0 | 44.0 | 260.0 |
| Short-Term Technical Assistance | | | | | |
| Short-Term Expatriate Advisors | 160.0 | 120.0 | 60.0 | 60.0 | 400.0 |
| Local Regional Consultants | 150.0 | 150.0 | 100.0 | 50.0 | 450.0 |
| Other Direct Costs | 100.0 | 125.0 | 125.0 | 125.0 | 475.0 |
| **Institutional Strengthening** | | | | | |
| UNASCU | 60.0 | 40.0 | 30.0 | 20.0 | 150.0 |
| Equipment Grant Facility | 20.0 | 20.0 | 15.0 | 15.0 | 70.0 |
| Capitalization Grant Facility | 40.0 | 40.0 | 20.0 | | 100.0 |
| Work Orders | | | | | |
| Training Program Development | 70.0 | 70.0 | 70.0 | 40.0 | 250.0 |
| Certification Program | 20.0 | 20.0 | | | 40.0 |
| Lobbying Activities | 30.0 | 30.0 | | | 60.0 |
| Training of Trainers | 30.0 | 30.0 | 20.0 | | 80.0 |
| **Participant Training** | 50.0 | 50.0 | 50.0 | | 150.0 |
| **Key Systems Development** | | | | | |
| Liquidity Fund | | 50.0 | 200.0 | | 250.0 |
| Stabilization Fund | | 50.0 | 200.0 | | 250.0 |
| Management Information System | 250.0 | 250.0 | | | 500.0 |
| Grand Total | | | | | 4,085.0 |

*USAID/Kiev should consider counterpart contribution in reviewing this full budget.

## STRATEGIC CONSIDERATIONS

Any activity that USAID/Kiev would undertake in support of credit unions would take place in an ongoing environment involving multiple donors. Coordination with other donors is crucial for ensuring unnecessary duplication of efforts, contradictory objectives, and competing interests. CIDA and USAID have been, and are likely to continue to be, the major donors, so proper coordination among these programs is absolutely essential. Other donors—such as the Soros Foundation, DFID, British Know How Fund, Eurasia Foundation, World Bank, EBRD, and others—may provide additional assistance to the movement, although on a lesser scale than the CIDA and USAID programs. The coordination that is required must take place among the donors themselves; the grantee or contract implementers of specific donor programs are not in a position to effect a coordinated strategy of assistance to the movement. In addition, a coordinating committee—comprised of representatives from the major donors, the board and chief executive of UNASCU, and the chiefs of party of the major support programs—should be established to set policy and coordinate activities to ensure that assistance properly benefits the Ukrainian credit union movement.

A USAID/Kiev activity in support of credit unions also involves the national credit union movement. When the implementation grant to WOCCU was initiated in 1995, the Ukrainian movement was just starting, and it lacked both the vision and experience to effectively design and coordinate a project. That is no longer the case. For any activity to be successful and achieve its objectives, the national movement must be involved in the project and must feel ownership of it. Ownership and involvement needs to take place in three ways:

*1. Activity Design.* The conclusions and recommendations of this report have been discussed with UNASCU officials. They are in basic agreement with these conclusions and recommendations. As the activity design process continues, however, and as the details of the activity become more developed, USAID/Kiev needs to involve UNASCU in reviewing and commenting on both the overall concept and objectives of the activity and the implementation strategies to make sure they are in agreement with these.

*2. Selection of Grantee.* Unless there is an apparent conflict of interest, UNASCU also should be consulted during the grantee evaluation and selection process, and comments from UNASCU should be taken seriously by USAID/Kiev officials in making the final selection. USAID/Kiev, of course, is responsible for final selection of the grantee, but cogent observations and suggestions by UNASCU need to be taken into account in that final selection.

*3. Project Implementation.* To avoid the types of conflicts that were present in the previous grant activity, UNASCU needs to be involved in and have a responsibility for coordinating project implementation. At a minimum, a steering committee consisting of two members of the UNASCU Board of Directors, and a representative from each of the major donors, with the chiefs of party and President of UNASCU acting as resources, should be established to guide the project and keep it on track.

# APPENDICES

## A. CONTACTS

### UNASCU

Petro M. Kozynets, President, Ukrainian National Association of Savings and Credit Unions, tel. 219-4486, unascu@fortress.kiev.ua

Andriy Y. Olenchik, Vice President and Director of Training and Methodological Center, tel. 210-4192, cutc@fortress.kiev.ua

Lyudmila E. Kravchenko, General Director, FORTRESS Insurance Company, tel. 246-6850, lkravchenko@fortress.kiev.ua, www.ukrcu.ua/fortress

Iryna Kozak, Regional Representative in Lviv central_cu@link.lviv.ua

### INTERNATIONAL PROJECTS

Bohdan Kozy, Project Manager, Ukraine Credit Union Development Assistance Program, Joint Project of the Canadian Co-operative Association and the Council of Ukrainian Credit Unions of Canada, tel. 229-4227, ucudap@gluk.org

Rostislav V. Haidayenko, Private Consultant, former head of WOCCU project in Ukraine, tel. 227-3985 or 7191, rosti@cazziez.kiev.ua

Lucy Ito, Project Director, World Council of Credit Unions, tel. 231-7130, lito@woccu.org

Bohdan Watral, President and CEO, Selfreliance Credit Union, Chicago, tel. (773) 489-0520

Tamara Denysenko, General Manager and CEO, Rochester Ukrainian Federal Credit Union, tel. (716) 544-9518, tamara.denysenko@gte.net

Ihor Eugene Lszok, President/CEO, Selfreliance UA Federal Credit Union, tel. (973) 373-7839

Marta Kolomayets, Team Leader, Ukraine Market Reform Education Project, tel. 044-490-69-88, PBNMartak@aol.com

Irina Movchan, Information Line Supervisor, Ukraine Market Reform Education Project, tel. 044-490-69-88, infoline@office.umrep.kiev.ua

## DONORS

Emil Baran, Counsellor/Conseiller, Canadian Embassy, Kiev, tel.464-1144, emil.baran@dfait-maeci.gc.ca

Steve Silcox, Chief, Private Sector Division, U.S. Agency for International Development, Kiev, tel. 044-462-5678, ssilcox@usaid.gov

Sergey A. Vetosh, Banking Specialist, U.S. Agency for International Development, Kiev, tel. 462-5678, svetosh@usaid.gov

Mary M. Lynch, M.M. Lynch Consultants International, Tel. (613)-226-7661, mmlci@netcom.ca

Aleksander Kaliberda, Economist, The World Bank, Kiev, akaliberda@worldbank.org

Olena Sichkar, National Programme Officer, United Nations Development Program, olenas@un.kiev.ua

Gennadyi Aksionov, International Foundation for Social Adaptation, Kiev, tel. 467-1204, aksionov@ifsa.kiev.ua

## CREDIT UNIONS

### Western Ukraine

Olha Maksymiv, Chairman, Executive Officer, and Credit Union Development Specialist for CCA and UNASCU, Samopomich Credit Union, Chortkiv (Ternopil Oblast), tel. (03552) 208-67, Olga@spomich.te.ua

Bogdan Sidorak, Chairman, Vygoda Credit Union, Stryi, tel. (03245) 510-86

Maria Suma, Executive Director, Vygoda Credit Union, Stryi, tel. (03245) 510-86
Volodymyr Sidorovskyi, Chairman and Executive Director, Aniciya Credit Union, Lviv, tel. (0322) 743-353

Maria Galonska, Executive Director, Vidrozhennia, Copchensi

Shakhorina Stanislava, Chairman and Executive Director, Tereboliya Credit Union, Tereboliya, tel. (03551) 229-46, vika@kster.ssft.net

### Kiev Region

Galina Robtsova, Executive Director, Credit Union FORT, Kiev, tel. 467-1204, aksionov@ifsa.kiev.ua

Ivan Duda, Chairman, Kiev Farmer's Credit Union, tel. 227-7258, farmer@ukrpack.net

Dmytro Miretsky, Credit Union Development Consultant, Kiev (works with Farmer's Credit Union)

Galina Zhulinska, Chairman, Credit Union Turbota, Kiev, tel. 228-7909

Olga Levchenko, Head of Credit Committee, Credit Union Turbota, Kiev, tel. 229-4912

**Eastern Region**

Tamara Byetyeva, Chairman, Tsentralna Credit Union, Dnipropetrovsk, tel. (0562) 341-435, cuc@cucentral.dp.ua

Oksana Mytsyk, Consultant in Accounting for UNASCU/CCA, Poltava, tel. (05322) 277-02, slspilka@kot.poltava.ua

Andrei Panteleimonenko, Chairman, Credit Union Kassa Vzaemodopomogyi, Poltava, tel. (05322) 277-02, slspilka@kot.poltava.ua

Sergei Goncharenko, Executive Director, Slobidska Credit Union, Kharkiv, tel. (0572) 478-143

Mikhail Varich, Deputy Chief of Commercial Department, Yuzhny Machine Building Plant, Dnipropetrovsk, tel. (0562) 322-300, Varich@solar.unity.net

Oleksander Sabrenko, Manager, Credit Union Kassa Vzaemodopomogyi, Poltava, tel. (05322) 277-02, slspilka@kot.poltava.ua

Miroslav Aliman, Assistant Professor, Poltava Cooperative Institute, Poltava, tel. 80-53-22

Nikolai Nikolaevich, Kredit Union Kirovitz, Dnipropetrovsk

Lilia Kim, Chairman of the Board, Zhinocha Vzaemodopomora, Kharkiv, tel. (0572) 920-030, lilia@wfound.kharkov.ua

Svetlana Astasheva, Executive Director, Zhinocha Vzaemodopomora, Kharkiv, tel. (0572) 920-030

Sergey Kartsev, Executive Director, Kharkiv Region Credit Society, Kharkiv

Tamara Tratsevitcha, Toloko, Kharkiv

Stanislav Filenko, Kassa Vzaemopomich, Kharkiv, tel. (0572) 23-66-58, iTL710@online.kharkov.ua

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# C. DRAFT SCOPE OF WORK

## Long-Term Advisor/Chief of Party

A Ukrainian-speaking expatriate advisor would be required to fill the role of Chief of Party for the first three years of this four-year project.

### General Duties and Responsibilities

The Chief of Party would be responsible for planning and implementing the program of assistance to UNASCU and the Ukrainian credit union movement, and would be responsible for meeting the performance targets established for the activity. The general activities and responsibilities for the Chief of Party are the following:

- Serving as a liaison with, and reporting to, USAID/Kiev;
- Working closely with the UNASCU chief executive and UNASCU staff and board to plan and implement an effective program of technical assistance, training and financing for the Ukrainian credit union movement;
- Preparing an annual operating plan in coordination and cooperation with UNASCU;
- Coordinating activities with those of other donors, especially advisors from any CIDA-financed project of support to UNASCU;
- Leading staff development and capacity building in the areas of public awareness, lobbying and advocacy, association management and operations, and strategic planning;
- Planning and coordinating the activities of short-term consultants;
- Supervising and managing the activities of local staff and consultants in such a manner that these enhance the image of UNASCU as a national membership organization; and
- Preparing required reports.

### Specific Tasks and Responsibilities

It is not possible to define all of the specific tasks that the Chief of Party will undertake and, as conditions and requirements may change over time, it is not advisable to either limit or constrain the ability of the Chief of Party to adapt the program of activities to meet the needs of a changing environment. Nevertheless, the immediate problems facing UNASCU and Ukrainian credit unions suggest general courses of action that the advisor must be prepared to address. These include:

- Plan and carry out with UNASCU a growth strategy to expand the movement into new cities and regions;

- Work with UNASCU and the Credit Union Training Center to develop management and internal control tools and procedures for credit unions;
- Plan and carry out, with UNASCU, a program to better monitor and assess the strengths and weaknesses of credit unions in the country, and to provide follow-up and support to help credit unions become more efficient and effective financial institutions;
- Assess, plan and direct a program to help credit unions resolve their data processing/information management problems and needs;
- Develop an effective strategic planning process for UNASCU and its member credit unions;
- Assist UNASCU with the planning and development of its core business areas, including training and the service center;
- Assist UNASCU to assess the feasibility of establishing a central liquidity facility and/or stabilization fund;
- Identify appropriate short term technical assistance or local service providers to assist with training curriculum development for credit union staff and management, training certification and training of trainers;
- Assist UNASCU with the preparation of five-year financial projections geared toward financial self-sufficiency through increased services for fees, increased member dues and other revenue generating activities;
- Assist with the development of an effective lobbying strategy for UNASCU vis-à-vis the national government and parliament that is focused on passing new legislation that provides an effective legal and regulatory framework for credit unions; and
- Work with UNASCU to improve its governance systems, including developing and expanding the use of committees as a way to resolve issues and increase participation of credit union members in the national association.

**Minimum Requirements**

The person filling this role would need to have the following qualifications:

- International work experience is preferred, but not required;
- Ukrainian-speaking expatriate;
- A minimum of five years of experience of experience in credit unions, with actual experience in both a management position in a successful growth-oriented credit union and experience in a credit union association.

Credit union experience is needed to be able to orient the program toward developing a vision of growth and service and for helping credit unions understand how to manage that growth. Credit union association experience is needed to be able to help UNASCU develop into an effective, service- and member-oriented national association.

In addition, the Chief of Party must have the personal and communications skills to work effectively in a role that helps UNASCU and the Ukrainian credit union movement grow and develop as an effective credit union system.

# D. SUMMARY OF CREDIT UNIONS VISITED

| Credit Union/Location | | STATISTICS | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | | No. Members (1/1/00) | Year Founded | Total Assets (1/1/00) | Real Asset Growth from 1/99 | Membership Requirements | Interest Rates–Deposits | Interest Rates–Loans | Financial Products | C | US | |
| 1 | **Farmer's Credit Union, Kiev** | 163 (27% women) | 1997 | 48,765 hryvna (60,000 April 2000) | 16.5% | • Farmer/member of farmer's family within Kiev oblast<br>• 20 hryvna fee; 200 hryvna min. share deposit | 44% on dividends<br>44% on deposits<br>4%/month | 4% month on declining balance; max. loan not to exceed 10% of total CU assets | • Ag. (77%) and consumer loans (13%)<br>• Primarily dividends, but also some deposits | X | | |
| 2 | **Turbota Women's Credit Union, Kiev** | 335 (67% women) | 1997 | 465,338 hryvna (650,000 April 2000) | 53.2% | • Recommendation of member<br>• Don't have to be a woman<br>• Live in Kiev oblast<br>• 10 hryvna membership fee | 24% on deposits, 27% on share dividends | 6% month on consumer loans, 4-5.5% on business loans | • Consumer and small business loans<br>• Share and savings deposits | | X | |
| 3 | **Fort Credit Union, Kiev** | 172 (33% women) | 1998 | 354,245 | 72.1% | • Recommendation of member<br>• Certificate of salary<br>• Live in Kiev city<br>• Was originally for retired military | Only shares deposits; have paid 36-42% on dividends | Larger loans 42%, short term 3% week | • Consumer, small business, short-term loans<br>• No ag. loans<br>• Only share deposits | | X | |

| | | No. Members (1/1/00) | Year Founded | Total Assets (1/1/00) | Real Asset Growth from 1/99 | Membership Requirements | Interest Rates–Deposit s | Interest Rates–Loans | Financial Products | C | US | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| 4 | **Anicija, Lviv** | 545 (46% women) | 1997 | 320,385 (390,000 April 2000) | -22.8% | • Membership to traditional Ukrainian church (orthodox or Ukrainian Catholic) | 40% on deposits; don't pay dividends yet | 5-8% month; demand is greater for loans than deposits; down from 10% | • Consumer, small business, and short-term loans<br>• Traditional deposits, pensions, and education savings | | X | |
| 5 | **Vygoda, Stri (Lviv Oblast)** | 2,071 (74% women) (2,500 April 2000) | 1992 | 379,930 | -8.6% | • Members are members of NGO Prosvita | 24-42% on deposits; no dividends paid | 72% on consumer loans, 66% education loans, 65% on housing construction loans, 60% on business loans | • Consumer health care, education, housing construction, business loans<br>• Deposits up to 3 months, up to 6 months, sight deposits, children's savings for orphans | X | X | |
| 6 | **Samopomich, Chortkiv (Ternopil Oblast)** | 1,486 (67% women) (1,640 in April 2000) | 1994 | 308,023 (365,000 April 2000) | -10% | • Members are from the Greek Catholic Church<br>• Members must live in the rayon<br>• 40% rural persons currently | 36-48% on deposits depending on term | 62% on consumer loans, 24% on ag. loans (but dep. rate for farmers is lower), 72% on SME loans | • Consumer (1.6 m), small business and ag. loans<br>• Deposit up to 3 months, 6 months, 1 year, sight deposits, children's savings | X | X | |

| | | No. Members (1/1/00) | Year Founded | Total Assets (1/1/00) | Real Asset Growth from 1/99 | Membership Requirements | Interest Rates–Deposits | Interest Rates–Loans | Financial Products | C | US | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| 7 | **Vidrozhennia, Capenchinsi (Ternopil Oblast)** | 297 (81% women) | 1997 | 62,754 (85,000 in April 2000) | 77.4% | • Member of Prosvita<br>• Citizens of the oblast | 48% for sight deposits; 60% for fixed term up to 6 months | 96% on all loans | • Consumer, ag., SME loans<br>• Sight and fixed term deposits | X | | |
| 8 | **Tereboliya Credit Union, Terboliya (Ternopil Oblast)** | 1,446 (61% women) | 1997 | 135,979 | 54.8% | • Members are from Prosvita and the intelligentsia | 36-60% annually depending on term of deposit | 96% annually on all types | • Consumer, ag., education, special occasion and SME loans<br>• Children's savings, fixed term, new deposits; no dividend payments | X | X | |
| 9 | **Tsentralny Credit Union, Dnipropetrovsk** | 1,437 (63% women) | 1998 | 229,226 | -51% | • Members are employees of Uzhmash and sister firm that does R&D | 35% on deposits; 40-50% on dividends paid quarterly | 40-60% short term cash loans, 24% on heath, 30-35% on health, 22% on consumer, 60% on SME | • Consumer, short-term cash, education, health, youth, and SME loans<br>• Share and sight deposits | | X | |
| 10 | **Kirovitz Credit Union, Dnipropetrovsk*** | 850 (approx. 50% women) | 1996 | 100,000 | N/A | • Members are employees of train building factory | 32% annually | 48% annually | • Consumer, short-term, special occasion and health care loans | | | |
| 11 | **Zhinocha Vzaemopomich, Kharkiv** | 116 (97% women) | 1997 | 34,987 | 39% | • Members are from the various women's organizations in the | 20% if deposit is large | 35-50% on loans, plus 3% on the total amount of | • Consumer, short-term, microenterprise, | | X | |